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AUDIT COMMITTEE
SUPPLEMENTARY AGENDA

28 January 2020

The following report is attached for consideration and is submitted with the agreement of the Chairman as an urgent matter pursuant to Section 100B (4) of the Local Government Act 1972

7 **TREASURY MANAGEMENT MID-YEAR UPDATE 2019-20** (Pages 1 - 16)

Report attached.

8 **TREASURY MANAGEMENT STRATEGY STATEMENT 2020/21** (Pages 17 - 50)

Report attached.

9 **GOVERNANCE & RISK UPDATE** (Pages 51 - 58)

Report and appendix attached.

10 **ACCOUNTING POLICIES - 19/20** (Pages 59 - 82)

Report and appendix attached.

11 **ASSURANCE PROGRESS REPORT** (Pages 83 - 98)

Report and appendices attached.

Andrew Beesley
Head of Democratic Services

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Havering
LONDON BOROUGH

AUDIT COMMITTEE	**28th January 2020**
Subject Heading:	**TREASURY MANAGEMENT MID YEAR UPDATE 2019-20**
SLT Lead:	**Jane West** **Chief Operating Officer**
Report Author and contact details:	**Zainab Roberts / Stephen Wild** **Treasury Manager / Head of Pensions and Treasury** **01708434306** **Zainab.Roberts@havering.gov.uk**
Policy context:	**The Code of Practice on Treasury Management (Revised 2017) requires that Council be provided with a mid-year report on treasury activities.**
Financial summary:	**There are no direct financial implications from the report.**

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[x]
Places making Havering	[x]
Places making Havering	[x]
Connections making Havering	[x]

Summary

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The Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management Code ("TM Code") require authorities to report on treasury management activities to Full Council at least twice per year (mid-year and at year end).

The Authority's Treasury Management Strategy Statement (TMSS) for 2019-20 was approved at a meeting of the Authority in February 2019.

The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers activity on treasury managed investments and borrowings and the associated monitoring and control of risk.

The key highlights of the Mid-Year report are as follows:

- At the end of December investment portfolio return was 1.068% outperforming the LINK benchmarking Group average of 0.98% and the authority's Budgeted rate of return of 0.80% against a backdrop of falling 3 month LIBOR.

- Gilt yields are currently low but on the 9th October the HM Treasury increased the current margin over gilt by 100bp (one percentage point). This was a policy decision by the Government directed at reducing the unprecedented growth in PWLB borrowing. London Local authorities have campaigned for the decision to be reversed. While the outlook on interest rates remains benign and the market is starting to develop cheaper alternatives to the PWLB, officers will continue to fund the authority's capital financing requirement from cheaper internal borrowing. In 2019-20 the Authority's investment income budget of £1.7m is set to be exceeded.

- There was no breach of the Authority's prudential indicators and treasury indicators.

RECOMMENDATIONS

- To note the treasury management activities to December 2019 are detailed in the report.

REPORT DETAIL

1. Background

Treasury management

1.1 The authority operates a balanced budget, which broadly means cash raised during the year will meet its cash expenditure. Part of the treasury management operation is to ensure this cash flow is adequately planned, with surplus monies being invested in low risk counterparties, providing adequate liquidity initially before considering optimising investment return.

1.2 The other main function of authority's treasury management operation is to help fund its capital plans. These capital plans provide a guide to the borrowing need of the authority, essentially the longer term cash flow planning required to meet its capital spending operations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

Capital Strategy

1.3 In December 2017, CIPFA published revised Prudential and Treasury Management Codes. As from 2019/20, all local authorities were required to prepare a Capital Strategy which is intended to provide the following: -

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability

1.4 A report setting out our Capital Strategy will be taken to the full council, (or cabinet, with responsibility retained by the full council), before 31st March 2020.

2. Introduction

2.1 This report has been written in accordance with the requirements of the CIPFA TM Code.

2.2 This is the Mid-Year Review Report required by the TM Code and covers the following:

- an economic update for the first part of the 2019/20 financial year

- Treasury Management Summary to December 2019
- a review of the authority's borrowing strategy for 2019/20
- a review of the authority's investment portfolio for 2019/20; and
- a review of compliance with Treasury and Prudential Limits for 2019/20.

3. Economics and interest rates

Economics update

3.1 The Bank of England Monetary Policy Committee ("MPC") has held its main interest rate steady at 0.75% with its rate-setting committee voting 7-2 in favour of keeping the current level.

The central bank maintained the dovish stance exhibited after its previous meeting, commenting in an accompanying statement: "If global growth fails to stabilize or Brexit uncertainties remain entrenched, monetary policy may need to reinforce the expected U.K. recovery."

Its forecast for U.K. GDP (gross domestic product) growth in the fourth quarter of 2019 was cut to +0.1% from the November forecast of +0.2%, reflecting the weakening of economic conditions shown in recent data.

Two MPC policymakers, Jonathan Haskel and Michael Saunders, voted to cut the main interest rate to 0.5%, as was also the case in November.

On the U.S.-China trade war, the Bank of England noted the "partial de-escalation of the U.S.-China trade war gives some additional support to the outlook" but highlighted that the continued sign of loosening in the U.K. labour market was another potential headwind.

The central bank has been grappling with uncertainty over Brexit for the past three years, and their focus now switches to what kind of trade deal the the U.K will negotiate with the EU.

Following the Conservative Party's election victory, which all but ensures the U.K. will leave the EU before the January 31 deadline, Prime Minister Johnson has vowed to block any extension to the post-exit transition period beyond the end of 2020.

Interest rate forecasts

3.2 The authority's treasury advisor, Link Asset Services (LAS), has provided the following forecast in table 1 below:

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Table 1: Interest Rate forecast

Bank Rate	NOW	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Link Asset Services	**0.75%**	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.25%
Capital Economics	**0.75%**	0.75%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	-	-	-	-	-
5yr PWLB Rate	**NOW**	**Mar-20**	**Jun-20**	**Sep-20**	**Dec-20**	**Mar-21**	**Jun-21**	**Sep-21**	**Dec-21**	**Mar-22**	**Jun-22**	**Sep-22**	**Dec-22**	**Mar-23**
Link Asset Services	**2.20%**	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.20%	3.20%
Capital Economics	**2.20%**	2.40%	2.50%	2.50%	2.60%	2.60%	2.80%	2.80%	2.90%	-	-	-	-	-
10yr PWLB Rate	**NOW**	**Mar-20**	**Jun-20**	**Sep-20**	**Dec-20**	**Mar-21**	**Jun-21**	**Sep-21**	**Dec-21**	**Mar-22**	**Jun-22**	**Sep-22**	**Dec-22**	**Mar-23**
Link Asset Services	**2.44%**	2.70%	2.70%	2.70%	2.80%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.50%
Capital Economics	**2.44%**	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.00%	3.10%	-	-	-	-	-
25yr PWLB Rate	**NOW**	**Mar-20**	**Jun-20**	**Sep-20**	**Dec-20**	**Mar-21**	**Jun-21**	**Sep-21**	**Dec-21**	**Mar-22**	**Jun-22**	**Sep-22**	**Dec-22**	**Mar-23**
Link Asset Services	**3.00%**	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.10%
Capital Economics	**3.00%**	3.10%	3.10%	3.20%	3.20%	3.20%	3.30%	3.30%	3.40%	-	-	-	-	-
50yr PWLB Rate	**NOW**	**Mar-20**	**Jun-20**	**Sep-20**	**Dec-20**	**Mar-21**	**Jun-21**	**Sep-21**	**Dec-21**	**Mar-22**	**Jun-22**	**Sep-22**	**Dec-22**	**Mar-23**
Link Asset Services	**2.85%**	3.20%	3.30%	3.30%	3.40%	3.50%	3.60%	3.60%	3.70%	3.80%	3.90%	3.90%	4.00%	4.00%
Capital Economics	**2.85%**	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%	3.40%	3.50%	-	-	-	-	-

4. Treasury Management Summary

4.1 The treasury management position as at 31st December 2019 and the change over the period is shown in table 2 below.

Table 2: Treasury Management Summary as at 31st December 2019

Investment Activity

	01.04.19 Balance	Movement	31.12.19 Balance	Weighted Average Rate %
Investments				
Fixed Deposit	138.100	-8.100	130.000	1.09
Money Market Funds	34.060	-23.180	10.880	0.73
Call Account	25.000	-10.000	15.000	0.90
Covered Bonds	4.000	-1.000	3.000	4.00
Total investments	**201.160**	**-42.280**	**158.880**	**1.10**

4.2 The authority's investments as at 31st December 2019 stood at £158.8m – consisting of £85m with local authorities, £68.8m with UK banks and £5m with non UK banks.

4.3 Appendix A shows the breakdown of the authority's investments.

4.4 Table 4 below shows the treasury investment performance for quarter ending 31st December 2019.

5. Borrowing Strategy

Borrowing Position

5.1 The 31st December 2019 borrowing position is shown in table 3 below.

Table 3: Borrowing Position

	Balance at 01.04.19 £m	Raised £m	Repaid £m	Balance at 31.12.19 £m	Weighted Average Rate %
Loans					
PWLB	203.234	-	-	203.234	**3.60**
Banks (LOBO)	7.000	-	-	7.000	**3.60**
Temporary Borrowing	0.351	15.000	-	15.351	**0.85**
Total Loans	**210.585**	**15.000**		**225.585**	3.40

5.2 The authority's capital financing requirement (CFR) for 2019/20 was forecast at £375m. The CFR denotes the Authority's underlying need to borrow for capital purposes. The Authority can borrow up to the CFR from PWLB or the market (external borrowing).

New borrowing

5.3 Affordability and the "cost of carry" remained important influences on the Authority's borrowing strategy alongside the consideration that, for any borrowing undertaken ahead of need, the proceeds would have to be invested in the money markets at rates of interest significantly lower than the cost of borrowing.

5.4 .

5.5 The gilt yields have been at their lowest but without warning on the 9th October 2019 PWLB increased the margin that applies to new borrowing from one to 2 percentage points with immediate effect.

As a result no long term borrowing has been undertaken in the year to date, but this will be kept under continuous review as capital investment plans are developed and spending is monitored.

Debt Rescheduling

5.6 The possibility of debt rescheduling is regularly discussed with our treasury adviser and is a regular agenda item at the quarterly treasury meeting held between the treasury officers, LAS, the S151 officer and the lead Member for Financial Management. However opportunities have been almost non-existent in the current economic climate.

LOBO's

5.7 The Authority holds a £7m LOBO loan, where the lender has the option to propose an increase in the interest rate at set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost.

6.0 Budgeted Income and Return

6.1 The Authority measures the financial performance of its treasury management activities both in terms of its impact on the revenue budget and its relationship to benchmark interest rates, as shown in table 4 below:

Table 4: 2019-20 Treasury Investment Performance to 31st December 2019

Period	Benchmark Return 3 month LIBOR (Average Quarterly Rate)	Budgeted Rate of Return %	Actual Rate of Return %	Investment Interest earned to Period end £m
Quarter 1	0.77	0.80	1.05	0.535
Quarter 2	0.75	0.80	1.06	0.519
Quarter 3	0.76	0.80	1.07	0.469
Average / Total				1.523

6.2 As shown in table 4, the authority outperformed its benchmark in all quarters. This was achieved by locking into longer term deposits to mitigate the impact of a falling 3 month LIBOR. However once these investments matured the cash becomes subject to current market rates.

6.3 It is expected that the average 3 months LIBOR will drop further and as maturing deposits are replaced with new investments at lower rates any excess interest in year may be eroded before the end of the financial year. Officers and LAS will consider reinvesting in longer duration investments (exceeding 364 days) and locking investments into forward deals to obtain higher yield (within existing risk parameters) subject to the authority's cash flow plan.

7.0 Current Investment Opportunities

7.1 The Authority is occasionally made aware of long term investment opportunities by other oneSource Authorities, brokers or investment advisers.

7.2 Cabinet on the 13th February 2019 approved changes to the Treasury Management Strategy Statement (TMSS) which facilitate investment in a wider range of products.

8.0 Money Market Fund Regulation (MMF)

8.1 Money Market Funds (MMFs) are an important source of short-term financing for financial institutions, corporates and governments.

8.2 On 30 June 2017, the MMFs regulation was published in the Official Journal of the EU. This regulation has two key objectives:

- Enhance financial stability within European markets by preventing the risk of contagion potentially transmitted by the "run" of MMFs to money markets and to their sponsors (mainly financial institutions)
- Increase investor protection by reducing the disadvantages for late redeemers in stressed market conditions.

8.3 This regulation introduces:

- New risk management requirements which impose stress testing and internal processes to determine credit quality for money market instruments, and "Know Your Customer" policies and procedures.

- New liquidity management requirements for Public Debt Constant Net Asset Value (CNAV) and Low Volatility Net Asset Value (LVNAV) MMFs. External support to guarantee the liquidity of an MMF or to stabilise its NAV are prohibited.

- These provide transparency requirements to investors and competent authorities.

So what does this all mean for Havering – have we using LVNAF MMFs now are we changing our specified investments?

9. Local Authority Lending

9.1 Over the last few years inter Local Authority lending and borrowing activity has gradually been increasing within the money markets. Whilst Local Authorities cannot provide a formal guarantee nor have the power to offer security they are required by statute to repay debt first out of revenues, before any spend, which is usually sufficient to give quasi UK Government ratings.

9.2 However over the last decade Local Authorities have faced significant financial pressures due to constant cuts in government funding on one hand and increasing demographic pressures on the other. Officers set overlay limits on lending to specific local authorities and where there are concerns then we may choose to remove them from our lending list.

9.3 LAS central view is that all local authorities have the same credit risk as the mechanisms that exist within the local authority legislative framework effectively prevent a local authority from going bankrupt.

This is reinforced by a statement from the National Audit Office, entitled Financial Sustainability of Local Authorities, dated November 2014, which states that:

“A legal framework at the core of the local government accountability system effectively prevents local authorities becoming insolvent. Local authorities cannot borrow to finance revenue expenditure or run deficits.”

10.0 Changes in risk appetite

10.1 The 2018 CIPFA Codes and guidance notes have placed enhanced importance on risk management. Where an authority changes its risk appetite e.g. for moving surplus cash into or out of certain types of investment funds or other types of investment instruments, this change in risk appetite and policy will be brought to members’ attention in treasury management update reports.

11.0 Compliance with Prudential and Treasury Indicators

11.1 It is a statutory duty for the Authority to determine and keep under review the affordable borrowing limits*.* The Authority's approved 2019/20 Treasury and Prudential Indicators (affordability limits) were included and approved by Full Council as part of the TMSS in February 2019.

11.2 During the half year, the Authority has operated within the treasury limits and Prudential Indicators set out in the authority TMSS and in compliance with the authority's Treasury Management Practices. An update on indicators and limits are reported in **Appendix B** of this report.

IMPLICATIONS AND RISKS

Financial implications and risks:

There are no direct financial implications arising from this report.

Legal implications and risks:

There are no apparent legal implications or risks from noting this report.

Human Resources implications and risks:

There are no HR implications from this report

Equalities implications and risks:

There are no Equalities implications arising from this report

BACKGROUND PAPERS

None

Appendix A

Table 1 breakdown of Deposits at 31st December 2019

Institution Type	1st April 2019 Actual £'m	31st December 2019 Actual £'m
UK Banks		
Goldman Sachs INT"L Bank	5.000	15.000
Lloyds Bank PLC	15.000	25.000
Santander UK PLC	20.000	15.000
Local Authorities & Other Public Sector		
Powys County Council	5.000	5.000
Lancashire County Council	5.000	5.000
Cambridgeshire County Council	5.000	5.000
Mid Suffolk District Council	5.000	5.000
London Borough of Haringey	4.000	
London Borough of Croydon	5.000	5.000
Gateshead Metropolitan Borough Council	5.000	
London Borough of Islington	5.000	5.000
Slough Borough Council	5.000	5.000
Newcastle Upon Tyne City Council	5.000	5.000
Northumberland County Council	10.000	10.000
Plymouth City Council	10.000	
Highland Council	5.000	
Telford and Wrekin Borough Council	5.000	
Dundee City Council	5.000	
Woking Borough Council	5.000	
London Borough of Barnet	5.000	
London Borough of Southwark		5.000
London Borough of Enfield		5.000
Eastleigh Council	5.000	
Warrington Borough Council		5.000
Aberdeenshire Council		5.000
Dunbartonshire Council		5.000
Salford City Council		5.000
Guildford Borough Council		5.000
Non UK Banks		
Australia		
Australia & New Zealand Banking Group	5.000	5.000
Netherlands		
Cooperative Rabobank	5.000	
Singapore		
Development Bank Singapore	5.000	
United State of America		
United Oversea Bank Ltd	4.100	
Money Market Funds		
Blackrock	4.060	
Federated Liquidity Sterling	15.000	7.820
Insight Investments Liquidity	15.000	3.060
Bond		

Rockfire capital Ltd	3.000	3.000
Covered Bond		
Santander (Floating rate note)	1.000	
TOTAL INVESTMENTS	**201.160**	**158.880**

Appendix B

Compliance Report

All treasury management activities undertaken during the half year complied fully with the CIPFA Code of Practice and the authority's approved Treasury Management Strategy. Compliance with specific treasury limits is demonstrated in tables below.

1.1 Interest Rate Exposures

1.1.1 This indicator is set to control the Authority's exposure to interest rate risk on its debt portfolio. The upper limits on fixed and variable rate interest rate exposures, expressed as the proportion of gross principal borrowed will be:

Table1: Interest rate exposure activity

	2019/20 Limit %	2019/20 Q3 Actual %	2020/21 Limit %	2021/22 Limit %
Upper limit on fixed interest rate exposure	100	96.60	100	100
Upper limit on variable interest rate exposure	25	3.40	30	35

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

1.1.2 Having larger amounts of fixed interest rate borrowing gives the Authority greater stability with regards to its interest payments and reduces the risk of higher interest costs should interest rates rise. Traditionally local authorities have taken advantage of fixing interest rates long term to reduce interest rate exposure. The table excludes Salix Finance loans as these are held at zero interest hence no interest rate exposure.

1.2 Maturity Structure of Borrowing

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

Table 2: Loan maturity structure

	Upper %	Lower %	Actual %
Under 12 months	40	0	6.65
12 months and within 24 months	60	0	0.00
24 months and within 5 years	80	0	0.49
5 years and within 10 years	100	0	25.06
10 years and above	100	0	67.80

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

1.3 Principal Sums Invested for Periods Longer than 365 days

1.3.1 The purpose of this indicator is to control the authority's exposure to the risk of incurring losses by seeking early repayment of its investments.

1.3.2 The limits set in the 2019/20 treasury management strategy in comparison to the half year are set below. It is the authority's policy to classify available for sale investments with maturities exceeding one year as short term investments.

Table 3: Investments for periods longer than 365 days

	2019/20 Limit £m	2019/20 Actual 31.12.19 at £m	2020/21 Limit £m
Limit on principal invested beyond year end	75	12.5	75

1.4 Gross Debt and the Capital Financing Requirement (CFR)

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

Table 4: Gross debt and the CFR

	31.03.19 Actual £m	31.03.20 Original Estimate £m	31.03.21 Revised Estimate £m	31.03.22 Estimate £m
Long Term External Debt	210.234	210.234	210.234	210.234
CFR	273.343	439.890	559.116	635.285
Internal Borrowing	63.109	229.505	348.882	425.051

1.4.2 Total debt is expected to remain below the CFR during the year. The actual debt levels are monitored against the Operational Boundary and authorised Limit for External Debt, below.

1.5 Operational Boundary for External Debt

1.5.1 The operational boundary is based on the authority's estimate of most likely, i.e. prudent, but not worst case scenario for external debt.

Table 5: Operational Boundary

Operational Boundary	2019/20 £m	2020/21 £m	2021/22 £m
Borrowing	423.000	436.000	468.000
Other long-term liabilities	10.000	10.000	10.000
Total	433.000	446.000	478.000

1.6 Authorised Limit for External Debt

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

Table 6: Authorised limit for external debt

Authorised Limit	**2019/20 £m**	**2020/21 £m**	**2021/22 £m**
Borrowing	472.000	487.000	520.000
Other long-term liabilities	10.000	10.000	10.000
Total Debt	472.000	497.000	530.000
Long Term Debt	210.385	210.385	210.385
Headroom	**261.615**	**286.615**	**319.615**

Glossary of Terms **Appendix C**

A bond is a debt instrument in which an investor lends money for a specified period of time at a fixed rate of interest. The issuing entity could be corporate, financial or government.

LIBOR?

A floating rate note (FRN) is a money market instrument with a Floating/variable rate of interest, which re-fixes over a reference rate, for example 3 month LIBOR.

Bail in is rescuing a financial institution on the brink of failure by making its creditors and depositors take a loss on their holdings. A **bail**-in is the opposite of a **bail**-out, which involves the rescue of a financial institution by external parties, typically governments using taxpayer's money.

Certificates of deposit (CDs) are a negotiable form of fixed deposit, ranked pari passu with fixed deposits. The difference is that you are not obligated to hold the CD to maturity, you can realise the cash by selling in the secondary market.

Coupon is the total amount of interest a security will pay. The coupon period depends on the security. A CD will often pay interest at maturity, while a bond may pay semi annually or annually and an FRN will most likely pay every 3 months.

Covered bond Covered bonds are conventional bonds (fixed or floating) issued by financial institutions, that are backed by a separate group of loans, usually prime residential mortgages. This lowers the creditor's exposure to default risk, enhancing the credit. This is why the issue is usually rated AAA, higher than the rating given to the issuer reduces exposure to bail-in risk.

Credit rating A measure of the credit worthiness of a borrower. A credit rating can be assigned to country, organisation or specific debt issue/ financial obligation. There are a number of credit ratings agencies but the main 3 are Standard & Poor's, Fitch or Moody's.

MIFID is the Markets in Financial Instruments Directive. A European Union Directive.

Principal is the total amount being borrowed or lent.

Spread is the difference between the buy and sell price of a security. It can also be the gap, usually in basis points, between the yield of a security and the benchmark security.

Treasury bills (T-bills) are UK government rated, short-dated form of Government debt, issued by the Debt Management Office (DMO) via a weekly tender. T-bills are normally issued for one, three or six month duration.

Havering
LONDON BOROUGH

AUDIT COMMITTEE	**28th January 2020**
Subject Heading:	Treasury Management Strategy Statement (TMSS) 2020/21 and Annual Investment Strategy (AIS) 2020/21, Treasury Indicators and Minimum Revenue Provision Policy Statement for 2020/21
SLT Lead:	Jane West Chief Operating Officer
Report Author and contact details:	Zainab Roberts / Stephen Wild Zainab.Roberts@havering.gov.uk Stephen.Wild@onesource.co.uk 01708 434 306 / 0203 373 3881
Policy context:	The code of practice on treasury management 2017 recommends that the Treasury Management Strategy and Minimum Revenue Provision Statement are reported to a scrutiny committee for effective scrutiny.
Financial summary:	The Treasury Management Strategy forms part of the Council's overall budget strategy and financial management framework.
Is this a Key Decision?	No
When should this matter be reviewed?	Bi-Annually
Reviewing OSC:	Audit Committee

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[x]
Places making Havering	[x]
Opportunities making Havering	[x]
Connections making Havering	[x]

SUMMARY

The TMSS and AIS are part of the Council's reporting procedures and are recommended by the Chartered Institute of Public Finance and Accountancy (CIPFA) code of practice on treasury management and its prudential code for capital finance in local authorities. The Local Government Act 2003 requires councils to comply with both codes.

This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the DCLG Guidance, and it covers:

- The Borrowing and Investment Strategies
- Treasury Management Indicators
- A Minimum Revenue Provision Policy (the means by which capital expenditure which is financed from borrowing is paid for by council tax payers)

RECOMMENDATIONS

Cabinet is asked to:

1. Approve the Treasury Management Strategy Statement (TMSS) 2020/21.
2. Approve the Treasury Management set out in Appendices 1 and 2 of this report.
3. Approve the Annual Minimum Revenue Provision (MRP) Statement for 2020/21 set out in Appendix 7 of this report.
4. Recommend the annual TMSS and MRP statements 2020/21 to Council for approval.
5. Delegate future changes required to this Strategy to the Chief Operating Officer in the consultation with the Cabinet Member for Finance and Property. This will provide the additional flexibility to swiftly respond to changing financial markets.

REPORT DETAIL

1. Introduction

1.1 The Authority is required to set a balanced budget each financial year, which broadly means that income received during the year will meet its operational expenditure. As part of the overall financial management arrangements, a primary objective of the Treasury Management service is to ensure that the Authority's cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in counterparties or instruments commensurate with the Authority's appetite for risk and liquidity requirements, as priorities before considering investment return.

1.2 Revised reporting is required for the 2020/21 reporting cycle due to revisions of the Ministry of Housing, Communities and Local Government (MHCLG) Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes include the introduction of a capital strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011.

CIPFA define treasury management as "The management of the local authority's borrowing, 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."

1.3 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities. This expenditure is shown throughout this report as "regeneration programme".

1.4 The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

a. **Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report is forward looking and covers:

- the capital plans, (including prudential indicators);
- (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).

b. **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c. **An annual treasury report** – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

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

2. Key Considerations and Sustainability

2.1 Treasury Management Strategy for 2020/21

2.1.1 The strategy for 2020/21 covers two main areas:

Capital issues

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

Treasury management issues

- the current treasury position; see table 1 below
- treasury indicators which limit the treasury risk and activities of the Council; Appendix 2
- prospects for interest rates; Appendix 3
- the borrowing strategy;
- policy on borrowing in advance of need; Appendix 4
- debt rescheduling;
- the investment strategy;
- creditworthiness policy;
- the policy on use of external service providers.

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

2.2 Training

2.2.1 One of the main requirements of the Treasury Code is the increased Member consideration of treasury management matters, and the need to ensure officers dealing with treasury management and investment are trained and keep their skills up to date. The Council addresses this important issue by:

- Providing training sessions, briefings and reports on treasury management and investment issues to those Members responsible for the monitoring and scrutiny of treasury management.
- This requires all relevant Officers to keep their skills up to date by utilising both external and internal training, workshops and seminars, and by participating in the CIPFA Treasury Management Forum and other relevant local groups and societies.

Treasury Management Consultants - The Council uses Link Asset Services as its external treasury management advisers. 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 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 agreed and subjected to regular review.

3. Service Delivery and Performance Issues

3.1 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, shown in Appendix 1, which are designed to assist Members' overview and confirm capital expenditure plans.

3.2 Current Portfolio Position

3.2.1 The overall treasury management portfolio as at 31 March 2019 and the position as at 31st December 2019 are shown below for both borrowing and investments.

Table1: Current Portfolio Position

	TREASURY PORTFOLIO			
	Actual 31/3/19 £m	**Actual 31/3/19 %**	**Current 31/12/19 £m**	**Current 31/12/19 %**
Treasury Investments				
Banks & Building Societies	60.100	32	60.000	38
Government (including Local Authorities)	109.000	58	85.000	53
Money Market funds	14.490	8	10.880	7
Bonds	3.000	2	3.000	2
Total Treasury Investments	**186.590**	**100**	**158.880**	**100**
Treasury External Borrowing				
Local Authorities				
PWLB	203.235	96	203.235	96
LOBO loans from banks	7.000	3	7.000	3
Other loans	0.351	1	0.351	1
Total External Borrowing	**210.586**	**100**	**210.586**	**100**
Net Treasury Investments/(Borrowing)	**(23.996)**		**(52.586)**	

3.2.2 The Council's forward projections for borrowing are summarised below in Table 2. The table shows the actual external debt, against the underlying capital borrowing need, (the Capital Financing Requirement - CFR), highlighting any over or under borrowing

Table 2: Capital Financing Requirement (CFR)

£m	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
External Debt					
Debt at 1 April	241	210	273	375	583
Expected change in Debt	(31)	63	102	208	115
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	**210**	**273**	**375**	**583**	**698**
The Capital Financing Requirement	**273**	**375**	**583**	**698**	**789**
Under / (over) borrowing	**63**	**102**	**208**	**115**	**91**

3.2.3 Within the above figures the level of debt relating to regeneration activities is detailed in table 3 below

Table 3: Regeneration Programme debt

	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
Actual debt at 31 March £m	26	57	181	214	229
Percentage of total CFR %	9	15	31	31	29

3.2.4 Within the range of prudential indicators there are a number of key indicators to ensure that the Council operates its activities within well-defined limits – see Appendix 1

3.2.5 The Chief Operating Officer reports that the Council complied with the prudential indicator that the Council's gross borrowing in the current year does not exceed its CFR and does not envisage difficulties for the future. This view takes into account current commitments, existing plans, and the proposals in this budget report.

3.3 Prospects for Interest Rates

3.3.1 Current Forecasts are shown in Appendix 3

3.3.2 The forecast anticipated consumer price inflation to remain around or slightly below 2% along with the expectation that the Bank of England will keep interest rates on hold at 0.75% until the situation on both Brexit and the global economy is clearer.

Our central case is that the EU withdrawal agreement will be approved by Parliament by the end of January 2020. The forecast assumes the Bank of England will raise interest rates to 1% in August 2020, and then remain on hold for the rest of the year. However, in a “no deal” scenario, we expect the Bank to cut the Bank Rate to near zero.

3.4 Borrowing Strategy

3.4.1 Caution will be adopted with the 2020/21 treasury operations. The Chief Operating Officer will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances.

3.4.2 The Council is currently maintaining an under-borrowed position. This means that the capital borrowing need (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Council’s reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

On the 9th October the PWLB unexpectedly announced that it was increasing its interest rates across all its new loans by 1% with immediate effect. Against this background and the risks within the economic forecast, caution will be adopted with the 2020/21 treasury operations. The Chief Operating Officer 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 an acceleration in the rate of increase in central rates in the USA and UK, an increase in world economic activity, or a sudden increase in inflation risks, then the portfolio position will be re-appraised. Most likely, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

3.4.5 **New Borrowing**

The council's borrowing strategy will give consideration to the following forms of borrowing to finance capital requirements:

- Internal borrowing: The need to undertake external borrowing can be reduced by the temporary use of internal balances held for provisions and reserves within the Council's accounts and cashflow movements on a day-to-day basis. The option of postponing borrowing and running down investment balances may provide short term revenue savings and reduce investment risk. The use of internal balances, however, must be monitored in order to mitigate the risks arising from the need to externally refinance when rates are unfavourable;
- Temporary Borrowing: from the money market or other local authorities;
- Shorter Term Borrowing (1 – 5 years): from non PWLB and other sources;
- Long Term Market Debt: where rates are significantly below those offered by the PWLB for an equivalent maturity period, and to provide diversity within the debt portfolio;
- PWLB: borrowing for periods across all durations where rates offer best value;
- Other borrowing arrangements: such as the use of leasing may be more cost efficient for some types of capital expenditure such as for vehicles and equipment.

3.4.6 The council will continue to borrow in respect of the following:

- Maturing debt;
- Approved (prudential) capital expenditure / capital investment;
- To finance short-term cashflow fluctuations.

3.4.7 The type, period, rate and timing of new borrowing will be determined by the Chief Operating Officer under delegated powers, taking into account the following factors:

- Expected movements in interest rates as outlined above;
- Maturity profile of the debt portfolio;
- The impact on the medium term financial strategy;
- Prudential indicators and limits.

Treasury Management Limits on borrowing activity

3.4.8. There are three debt related treasury activity limits. The purpose of these are to manage the activity of the treasury function within a flexibly set remit for risk management, yet not impose undue restraints that constrict opportunities for cost reduction or performance improvement. The indicators are:

- Upper limits on variable interest rate exposure net of investments;
- Upper limits on fixed interest rate exposure;
- Maturity structure of borrowing to manage refinancing risk.

3.4.9. The proposed indicators are set out in Annex C.

Policy on borrowing in advance of need

3.4.10. The Council must ensure that its total debt does not, except in the short-term, exceed the total of the CFR in the preceding year i.e. 2020/21, plus the estimates of any additional CFR for the year 2019/20 and the following two financial years. This allows some flexibility for early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

Any decision to borrow in advance will be considered carefully to ensure that value for money can be demonstrated, and that the Council can ensure the security of such funds.

In determining whether borrowing will be undertaken in advance of need the Council will:

- Ensure that the ongoing revenue liabilities created, and the implications for future capital plans and budgets have been considered;
- Evaluate economic and market factors that might influence the manner and timing of the decision to borrow;
- Consider the pros and cons of alternative forms of funding, interest rate structures and repayment profiles;
- Consider the positive and negative impacts of borrowing in advance of need on the Council's cash balances, in particular the increased exposure to credit risk that will arise as a result of investing this additional cash in advance of need.

3.4.11 **Debt Rescheduling**

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

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;
- To fulfil the treasury strategy;

- To 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.

3.5 Annual Investment Strategy

3.5.1 The MHCLG and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with financial investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy, (a separate report) which will be considered at the same meeting.

3.5.2 The Council's investment policy has regard to the following: -

- MHCLG's Guidance on Local Government Investments ("the Guidance")
- CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes 2017 ("the Code")
- CIPFA Treasury Management Guidance Notes 2018.

3.5.3 The key intention of the Guidance is to maintain the requirement for councils to invest prudently and that priority is given to the security and liquidity of investments before yield.
The Council's objective is therefore to achieve, within this constraint, the optimum return on its investments with the appropriate levels of security and liquidity.
Within the prudent management of its financial affairs, the Council may temporarily invest funds that are borrowed for the purpose of expenditure expected to be incurred in the reasonably near future. Borrowing purely to invest or on-lend for speculative purposes remains unlawful and the Council will not engage in such activity.

3.5.4 The above guidance from the MHCLG and CIPFA place a high priority on the management of risk. This Authority has adopted a prudent approach to managing risk, its minimum credit criteria is set out in Appendix 5.

3.5.5 The Council will consider placing longer term treasury deals while investment rates are at historically low levels and where attractive interest rates with high quality counterparties become available.

3.5.6 Investments will make reference to the core balance, cash flow requirements and the outlook for short and medium term interest rates.

3.5.7 Credit ratings should not be the sole determinant of the quality of an institution, this Council is not bound by the agency with the lowest rating and, importantly, officers will continually assess and monitor the financial sector and the economic/political environment in which institutions operate.

3.5.8 Treasury investment instruments identified for use in the financial year are listed in Appendix 6 under the ‘specified’ and ‘non-specified’ investment categories.

3.5.9 The Chief Operating Officer will, on advice, make operational changes to these limits in response to prevailing market conditions and regulatory changes.

3.5.10 All investments will be denominated in sterling.

3.5.11 As a result of the change in accounting standards for 2018/19 under IFRS 9, this authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund.

3.5.12 Following the consultation undertaken by the MHCLG on IFRS 9 the Government introduced a mandatory statutory override for local authorities to reverse out all unrealised fair value movements resulting from pooled investment funds. This was effective from 1 April 2018. The statutory override applies for five years from this date. Local authorities are required to disclose the net impact of the unrealised fair value movements in a separate unusable reserve throughout the duration of the override in order for the Government to keep the override under review and to maintain a form of transparency.

3.5.13 The largest UK banks, (those with more than £25bn of retail / Small and Medium-sized Enterprise (SME) deposits), were required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as “ring-fencing”. Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up.

3.5.14 Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and SME deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank (RFB) will be focused on lower risk, day-to-day core transactions, whilst more complex and “riskier” activities are required to be housed in a separate entity, a non-ring-fenced bank (NRFB). This is intended to ensure that an entity’s core activities are not adversely affected by the acts or omissions of other members of its group.

3.5.15 Whilst the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Council will continue to assess the new-formed entities in the same way that it does others and those with sufficiently high ratings, (and any other metrics considered), will be considered for investment purposes.

3.5.16 This Authority will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

3.5.17 The local benchmark for investment is the 3 month LIBOR rate.

3.6 Loans to Third Parties

3.6.1 The Authority may borrow to make grants or loans to third parties for the purpose of capital expenditure, as allowable under paragraph 25 (1) (b) of the Local Authorities (Capital Financing and Accounting) (England) Regulations 2003 (Statutory Instrument No. 3146). This facility is likely to be used to support local economic regeneration and development activity but not limited to those purposes. The additional capital expenditure may be funded by external borrowing. Loans for working capital or revenue purposes are permitted as long as these are funded from the Council's internal cash balances as external borrowing is not permitted in such circumstances.

3.6.2 **Pension Fund Cash** - The Local Government Pension Scheme (Management and Investment) Regulations 2016 requires the Council to maintain a separate bank account for the Pension Fund. For the management of Pension Fund cash, there is in place an agreement to pool internally held pension fund balances (working cash and those pending external investment) with the investment balances of the Council. These balances are invested in accordance with the Council's Treasury Management Strategy.
The Pension Fund receives interest annually on their cash balances at a rate commensurate with that received by the Council. Pension Fund cash balances may be withdrawn anytime. In the event of loss of any investment, this will be borne on a pro rata basis equivalent to the value of each party's contribution to the investment which incurred the loss.

3.6.3 **Pension Fund Prefunding** – The Council can choose to enter into an agreement to made advance payment to fund the employee pension contribution for up to 3 years. The benefit of this is to take advantage of discount rate provided by the Pension Fund Actuary which will results in cash saving for the Council. The Council has not previously adopted such advance payments.

3.7 Treasury Indicators

3.7.1 The indicators cover 2018/19 -2022/23. The CIPFA Prudential Code and the TM code requires authorities to set treasury indicators and these are set out in Appendix 2. No breaches in the indicators are expected in 2019/20.

3.8 Minimum Revenue Provision (MRP)

3.8.1 The MRP Policy Statement 2020/21 is set out in Appendix 7 of this report.

3.9 Policy on the use of external service providers

3.9.1 The Council uses Link Asset Services as its external treasury management advisors.

3.9.2 The Council recognises that responsibility for treasury management decisions remains with the organisation at all times. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

REASONS AND OPTIONS

Reasons for the decision:

The statutory Codes set out that the Council ought to approve a Treasury Management Strategy Statement, the MRP Strategy and the Prudential Indicators.

Other options considered:

The MHCLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Chief Operating Officer, having consulted the Cabinet Member for Finance and Property, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

Alternative	Impact on income and expenditure	Impact on risk management

Invest in a narrower range of counterparties and/or for shorter times	Interest income will be lower	Lower chance of losses from credit related defaults, but any such losses may be greater
Invest in a wider range of counterparties and/or for longer times	Interest income will be higher	Increased risk of losses from credit related defaults, but any such losses may be smaller
Borrow additional sums at long-term fixed interest rates	Debt interest costs will rise; this is unlikely to be offset by higher investment income	Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs may be more certain
Borrow short-term or variable loans instead of long-term fixed rates	Debt interest costs will initially be lower	Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long-term costs may be less certain

IMPLICATIONS AND RISKS

Financial implications and risks:

The Treasury Management Strategy Statement is a key part of the overall budget strategy and financial management framework and governs the strategic and operational treasury management activities throughout each financial year in order to manage the Council's financial risks associated with cash management via borrowing and investments.

For the financial year 2020/21, the budget for investment income has been set at £1.7m, based on an average interest rate of 0.8%.

The budget for long term debt interest payable in 2020/21 has been increased from £10.5m to £13.2m. This is based on the existing average long term debt portfolio of £210m at an average interest rate of 3.6% and has been adjusted for anticipated borrowing for the 2020/21 capital programme.

Of the existing £210m of long term debt, £174m is in relation to the HRA, with a budget for debt interest payable of £5.8m.

The General Fund Budget for debt interest on external debt has been increased from £2.4m to £5.1m to allow for external borrowing to be undertaken should it be considered necessary in 2020/21 to fund the cost of borrowing for the increased capital programme.

If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondingly different. Variance from budget will be reported on a bi-annual basis to full Council.

Legal implications and risks:

The Council must comply with its duty under section 3 Local Government Act 2003 to keep under review the amount of money the Authority can afford to borrow. Regulation 2 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003/3146 requires the Authority to have regard to the code of practice entitled the "Prudential Code for Capital Finance in Local Authorities" published by CIPFA when considering its duty under section 3.

The Council has fiduciary duties toward its tax payers to act in good faith in the interests of those tax payers with the considerable sums of money at their disposal. The Strategies being proposed for approval seek to discharge those duties in a reasonable and prudent fashion and therefore there is a low risk of successful challenge.

Otherwise there are no apparent legal implications arising as a result of this Report."

Human Resources implications and risks:

There are no direct Human Resources implications arising as a result of this report

Equalities implications and risks:

There are no equalities implications within this report

BACKGROUND PAPERS

- London Borough of Havering – Treasury management strategy 2020/21 and MRP Policy statement.

Appendix 1

PRUDENTIAL INDICATORS

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	2018/19 Actual	2019/20 Budget	2020/21 Budget	2021/22 Budget	2022/23 Budget
Non-HRA	**30.275**	**116.080**	**118.979**	**15.048**	**9.388**
HRA	**33.677**	**136.080**	**87.204**	**113.626**	**125.854**
Regeneration Programme *	**7.635**	**31.097**	**223.468**	**98.212**	**57.303**
Total	**71.588**	**283.257**	**429.651**	**226.886**	**192.545**

* these activities relate to areas such as capital expenditure on investment properties, loans to third parties etc.

Other long-term liabilities - The above financing need excludes other long-term liabilities that already include borrowing instruments.

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.

Financing of capital expenditure £m	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
Capital receipts	20.547	45.391	121.716	56.460	31.053
Capital grants	16.296	45.391	77.700	21.172	36.267
Revenue and Reserves	23.996	98.089	18.219	20.778	17.988
Net financing need for the year	**10.748**	**94.386**	**212.016**	**128.476**	**107.237**

The net financing need for regeneration programme activities included in the above table against expenditure is shown below:

Regeneration Programme £m	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
Capital Expenditure	8.785	28.097	223.468	98.212	57.303
Other Sources of Financing	0	0	98.250	55.000	30.000

Net financing need for the year	**8.785**	**28.097**	**125.218**	**43.212**	**27.303**
Percentage of total net financing need %	**81.74**	**29.77**	**59.06**	**33.63**	**25.46**

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 indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for (e.g. by capital grants), through a revenue or capital resource, 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 indebtedness in line with each assets life, and so charges the economic consumption of capital assets as they are used.

The CFR includes any other long-term liabilities (OLTL) which relates to PFI scheme and finance leases. The Council currently has no such liabilities within the CFR.

The Council is asked to approve the CFR projections below:

£m	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
Capital Financing Requirement					
CFR – non housing	72.185	105.360	152.225	163.405	169.187
CFR – housing	174.669	212.660	249.521	320.561	391.107
CFR – Regeneration Programme	26.489	56.985	181.158	214.454	229.156
Total CFR	**273.343**	**375.005**	**582.904**	**698.420**	**789.450**
Movement in CFR	**8.873**	**101.662**	**207.899**	**115.516**	**91.030**

Movement in CFR represented by					
Net financing need for the year	10.478	94.386	212.016	128.476	107.237
Less MRP and other financing movements	1.875	7.276	4.117	2.960	16.207
Movement in CFR	**8.873**	**101.662**	**207.899**	**115.516**	**91.030**

A key aspect of the regulatory and professional guidance is that elected members are aware of the size and scope of any commercial activity in relation to the authority's overall financial position. The capital expenditure figures and the details above demonstrate the scope of this activity and, by approving these figures, consider the scale proportionate to the Authority's remaining activity.

Within the range of 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 2020/21 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 or speculative purposes.

The Chief Operating Officers 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.

Core funds and expected investment balances

The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.).

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.

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 indicator:

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.

%	2018/19 Actual	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate	2022/23 Estimate
Non-HRA	2.47	3.24	5.24	5.47	5.95
HRA	3.81	4.65	5.45	7.00	8.55
Regeneration Programme	0.85	1.62	6.53	8.73	9.45
Total	7.13	9.50	17.22	21.21	23.94

Prior to 2018/19 regeneration programme activities are not shown separately in this table

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

Appendix 2

TREASURY INDICATORS

The Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the Capital Financing Requirement (CFR) in the preceding year plus the estimates of any additional CFR for 2019/20 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 or speculative purposes.

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 and the ability to fund under-borrowing by other cash resources.

Operational boundary £m	2019/20 Limit	2020/21 Limit	2021/22 Limit	2022/23 Limit
Debt	300	465	558	631
Other long term liabilities	10	10	10	10
Regeneration Programme	45	145	171	183
Total	355	620	739	824

The authorised limit for external debt

This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal 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 £m	2019/20 Limit	2020/21 Limit	2021/22 Limit	2022/23 Limit
Debt	450	698	837	946
Other long term liabilities	10	10	10	10
Regeneration Programme	67	217	257	275
Total	527	925	1104	1231

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 opportunities to reduce costs/improve performance.

The Code requires that for LOBO loans the maturity date is now deemed to be the next call date.

The indicators are:

Maturity structure of borrowing

These gross limits are set to reduce the Council's exposure of large fixed rate sums falling due for refinancing; these have been kept deliberately wide to provide flexibility for any restructuring that might be carried out to de-risk the debt portfolio.

Maturity structure of fixed interest rate borrowing 2020/21		
	Lower	**Upper**
Under 12 months	0%	40%
12 months to 2 years	0%	60%
2 years to 5 years	0%	70%
5 years to 10 years	0%	80%
10 years to 20 years	0%	100%
20 years to 30 years	0%	100%
30 years to 40 years	0%	100%
40 years to 50 years	0%	100%
Maturity structure of variable interest rate borrowing 2020/21		
	Lower	Upper

Under 12 months	0%	90%
12 months to 2 years	0%	90%
2 years to 5 years	0%	100%
5 years to 10 years	0%	100%
10 years to 20 years	0%	100%
20 years to 30 years	0%	100%
30 years to 40 years	0%	100%
40 years to 50 years	0%	100%

Investment treasury indicator and limit

Total principal funds invested for greater than 365 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 following treasury indicator and limit:

Upper limit for principal sums invested for longer than 365 days			
£m	**2019/20**	**2020/21**	**2021/22**
Principal sums invested for longer than 365 days	£75m	£75m	£75m

Appendix 3

PROSPECTS FOR INTEREST RATES

The Council has appointed Link 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 their central view.

Bank Rate														
	NOW	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Link Asset Services	**0.75%**	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.25%
Capital Economics	**0.75%**	0.75%	0.75%	0.75%	0.75%	0.75%	1.00%	1.00%	1.00%	-	-	-	-	-
5yr PWLB Rate														
	NOW	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Link Asset Services	**2.20%**	2.40%	2.40%	2.50%	2.50%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.20%	3.20%
Capital Economics	**2.20%**	2.40%	2.50%	2.50%	2.60%	2.60%	2.80%	2.80%	2.90%	-	-	-	-	-
10yr PWLB Rate														
	NOW	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Link Asset Services	**2.44%**	2.70%	2.70%	2.70%	2.80%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.30%	3.40%	3.50%
Capital Economics	**2.44%**	2.70%	2.70%	2.80%	2.80%	2.90%	3.00%	3.00%	3.10%	-	-	-	-	-
25yr PWLB Rate														
	NOW	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Link Asset Services	**3.00%**	3.30%	3.40%	3.40%	3.50%	3.60%	3.70%	3.70%	3.80%	3.90%	4.00%	4.00%	4.10%	4.10%
Capital Economics	**3.00%**	3.10%	3.10%	3.20%	3.20%	3.20%	3.30%	3.30%	3.40%	-	-	-	-	-
50yr PWLB Rate														
	NOW	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23
Link Asset Services	**2.85%**	3.20%	3.30%	3.30%	3.40%	3.50%	3.60%	3.60%	3.70%	3.80%	3.90%	3.90%	4.00%	4.00%
Capital Economics	**2.85%**	3.10%	3.10%	3.20%	3.20%	3.30%	3.40%	3.40%	3.50%	-	-	-	-	-

The Bank of England Monetary Policy Committee ("MPC") has held its main interest rate steady at 0.75% with its rate-setting committee voting 7-2 in favour of keeping the current level.

The central bank maintained the dovish stance exhibited after its previous meeting, commenting in an accompanying statement: "If global growth fails to stabilize or Brexit uncertainties remain entrenched, monetary policy may need to reinforce the expected U.K. recovery."

Its forecast for U.K. GDP (gross domestic product) growth in the fourth quarter of 2019 was cut to +0.1% from the November forecast of +0.2%, reflecting the weakening of economic conditions shown in recent data.

Two MPC policymakers, Jonathan Haskel and Michael Saunders, voted to cut the main interest rate to 0.5%, as was also the case in November.

On the U.S.-China trade war, the Bank of England noted the "partial de-escalation of the U.S.-China trade war gives some additional support to the outlook" but highlighted that the continued sign of loosening in the U.K. labour market was another potential headwind.

The central bank has been grappling with uncertainty over Brexit for the past three years, and their focus now switches to what kind of trade deal the the U.K will negotiate with the EU.

Following the Conservative Party's election victory, which all but ensures the U.K. will leave the EU before the January 31 deadline, Prime Minister Johnson has vowed to block any extension to the post-exit transition period beyond the end of 2020.

After raising rates in August 2018 to 0.75%, the MPC voted unanimously to hold rates during their September 2019 Policy meeting, reaffirming its pledge to gradual and limited rate rises under the assumption of a smooth Brexit and some recovery in global growth.
In August's Inflation Report, the BoE predicted a gradual increase in inflationary pressures, reaching above the inflation target of 2% by Q4 2020, and they forecast GDP growth to reach around 2.5% in 2022. Meanwhile, unemployment is expected to increase steadily up until Q3 2020, gradually decreasing from then on.

The US economy grew by an annualised 2.0% in Q2 2019, slightly below a preliminary estimate of 2.1% percent and following a 3.1% expansion in the previous three-month period, the second estimate showed.

The Fed decided to cut rates further by 25bps, lowering their target range to 1.75-2.00% during its September meeting, amid concerns about slowing global growth and trade wars.

On the 9th October 2019, the PWLB unexpectedly announced that it was increasing its interest rates across all its new loans by 1% with immediate effect.
While the Council's treasury management strategy permitted borrowing from a number of sources "it was not anticipated that any alternatives to PWLB would be utilised given the low cost of PWLB funding previously".

A further attraction of the PWLB had been "the low administration cost associated with raising funding, which was done by a simple phone call from officers when new borrowing was arranged".

The "significantly elevated resourcing requirement" of dealing with other lenders would depend on whether the currently underdeveloped market for lending to councils expanded now that the PWLB's rates were less attractive.

"The market which provides alternative funding to the PWLB for local authorities is not well developed,".

"Only a handful of authorities have raised funds via alternative routes, as PWLB rates have previously been at levels that competitors could not offer. This is now likely to change, and the market is likely to reassess the possibility of lending to councils."
The treasury team is liaising with LINK (the Council's Treasury Advisers) for alternative options to PWLB. e.g Pension Fund, LA to LA market, SPV etc.

Appendix 4

POLICY ON BORROWING IN ADVANCE OF NEED

The Council must ensure that its total debt does not, except in the short-term, exceed the total of the CFR in the preceding year i.e. 2020/21, plus the estimates of any additional CFR for the year 2019/20 and the following two financial years. This allows some flexibility for early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.
Any decision to borrow in advance will be considered carefully to ensure that value for money can be demonstrated, and that the Council can ensure the security of such funds.
In determining whether borrowing will be undertaken in advance of need the Council will:
• Ensure that the ongoing revenue liabilities created, and the implications for future capital plans and budgets have been considered;

- Evaluate economic and market factors that might influence the manner and timing of the decision to borrow;
- Consider the pros and cons of alternative forms of funding, interest rate structures and repayment profiles;
- Consider the positive and negative impacts of borrowing in advance of need on the Council's cash balances, in particular the increased exposure to credit risk that will arise as a result of investing this additional cash in advance of need.

Appendix 5

The Council's minimum credit ratings criteria

Credit Rating: Investment decisions are made by reference to the lowest appropriate published credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

Within the parameters set out below the Council works together with Link Asset Services (the treasury management advisor) to establish an operational lending list using Link's creditworthiness methodology.

The notes below should be read in conjunction with table 1 overleaf.

1. **Banks (Unsecured) and Building Societies**: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

   For non UK Banks, the Authority's credit criteria will require that banks from AA+ rated countries and above can be used.

   Current bank accounts: the Authority's own banker, Should the credit rating fall below A-, for liquidity purposes the Authority may continue to deposit surplus cash with the group providing that investments can be withdrawn on the next working day. Balances will be reviewed on a daily basis to assess their appropriateness.
   Banks (secured): Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in.

Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits.

The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

2. **Rated Building Societies -** The Authority's credit rating criteria for UK Building Societies in 2019/20 will continue to limit deposits to those UK Building Societies that meet the credit criteria in table 1 below.

3. **Non Rated Building Societies –** The criteria in table 1 overleaf will apply.

4. **Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

5. **Corporates:** Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made following an external credit assessment as part of a diversified pool in order to spread the risk widely.

6. **Registered providers:** Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing, formerly known as housing associations. These bodies are tightly regulated by the Regulator of Social Housing and, as providers of public services, they retain the likelihood of receiving government support if needed.

7. **Residential Mortgage Based Schemes** - Investment will be restricted to AAA rated funds with only UK exposure. These funds offer stronger risk-adjusted returns whilst maintaining high daily liquidity with time plus two days (T+2) access.

8. **Pooled funds:** Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee.

9. **Money Market Funds (MMF):** The Authority will continue to use MMF's, which provide lower interest returns but do provide a highly liquid, diversified investment via a highly credit-rated pooled investment vehicle.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.

Table 1: Approved investment counterparties and limits

Credit rating	Banks unsecured*	Banks secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£35m 5 years	£35m 20 years	£35m 50 years	£15m 20 years	£15m 20 years
AA+	£35m 5 years	£35m 10 years	£35m 25 years	£15m 10 years	£15m 10 years
AA	£35m 4 years	£35m 5 years	n/a	£15m 5 years	£15m 10 years
AA-	£35m 3 years	£35m 4 years	n/a	£15m 4 years	£15m 10 years
A+	£35m 2 years	£35m 3 years	n/a	£25m 3 years	£15m 5 years
A	£35m 13 months	£35m 2 years	n/a	£25m 2 years	£15m 5 years
A-	£35m 6 months	£35m 13 months	n/a	£15m 13 months	£15m 5 years
None	£1m 6 months	n/a	n/a	£5m 5 years	£10m 5 years
	UK Local Authorities £35m per authority; 50 years				
Pooled funds	£25m per fund These include Bond Funds, Gilt Funds, Equity, Enhanced Cash Funds, Mixed Asset Funds and Money Market Funds, Residential Mortgage Based Schemes (RMBS)				

* Includes Building Societies

Investment Limits

The Authority further proposes the investment limits as set out in the table below to protect the security of its investments. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 2: Investment limits

	Cash limit
UK Central Government	unlimited
Any single organisation, except the UK Central Government	£35m each
Any group of organisations under the same ownership	£35m per group
Any group of pooled funds under the same management	£35m per manager
Financial instruments held in a broker's nominee account	£50m per broker
Foreign countries	£35m per country
Registered providers	£35m in total
Unsecured investments with building societies	£50m in total
Loans to unrated corporates	£35m in total
Money Market Funds	£50m in total
UK Residential Mortgage Backed Securities (RMBS)	£25m in total

Appendix 6

Specified and Non Specified Investments

Specified investments:

The MHCLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
  - the UK Government,
  - a UK local authority, parish council or community council, or
  - a body or investment scheme of "high credit quality".

The Authority defines "high credit quality" organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds "high credit quality" is defined as those having a credit rating of A- or higher.

Limits on specified investments are shown in table 1 below.

Table 1: Specified Investments

Instrument	Institution Type	Instrument Minimum 'High' Credit Criteria	Limits	Max. Maturity Period
Accounts, deposits, certificates of deposit and senior unsecured bonds with banks other than multilateral development banks, UK Government Gilts.	UK Banks and UK Banking Groups[1]	per Appendix 5, Table 1	£35m	per Appendix 5, Table 1
	UK Building Societies	per Appendix 5, Table 1	£35m	per Appendix 5, Table 1
	Non UK Banks	Sovereign Rating of AA+ and above and meet Credit Criteria in Appendix 5, Table 1	£35m	per Appendix 5, Table 1
Covered bonds, floating rate notes, reverse repurchase agreements and other collateralised arrangements with banks and building societies	UK Banks and Building Societies and Non UK Banks	Per Appendix 5, Table 1 (and Sovereign Rating of AA+ minimum for Non UK Banks)	See Note 2	per Appendix 5, Table 1
Term Deposits	Local Authorities and other Public Institutions	UK Sovereign Rating	£35m	per Appendix 5, Table 1
Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing.	Registered Social Housing Providers	per Appendix 5, Table 1		per Appendix 5, Table 1
Money Market Fund		AAA [3]	£25m	
Enhanced Cash Funds		AA/Aa[4]	£25m	
Residential Mortgage Based Schemes (RMBS)		UK AAA	£25m	

1. £35m Limit per bank / banking group.
2. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.
3. Investments will be made with those MMF's which have a rating of AAA
4. Minimum of Fitch / Standard & Poor's AA or Moody's Aa rating

Non-specified investments:

Any investment not meeting the definition of a specified investment is classed as non-specified. The Authority does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality.

Limits on non-specified investments are shown in table 2 below.

Table 2: Non-specified investment limits

	Cash Limit £m
Total long-term investments	75
Total Investments without credit ratings or rated below A- (subject to due diligence)	20
Total non-specified investments	**95**

NON SPECIFIED INVESTMENTS

Instruments	Non Specified Investments	Institution Type	Minimum Credit Criteria	Maximum Duration	Cash limit
Accounts, deposits, certificates of deposit, structured deposits and senior unsecured bonds with banks other than multilateral development banks. Covered bonds, reverse repurchase agreements, and other collateralised arrangements with banks and building societies. Short Dated Bond Funds, Diversified Growth Funds, Absolute Return Funds and Property Funds. Unrated Bonds.	Total long-term investments (investments over 1 year)	UK and Non UK Banks and Building Societies, Rated Registered Social Housing Providers (RSP)	Per Appendix 5, Table 1	10 yrs.	£75m
	Total investments without credit ratings or rated below A- (except UK Government and local authorities)	Unrated Registered Social Housing Providers (RSP), Unrated Banks and Building Societies	N/A	5 yrs.	£20m
	Total Investments made in pooled investment vehicles.			7 yrs.	
	Total Investments made in un-rated bonds.				
	Total non-specified investments				**£95m**

Appendix 7

Minimum Revenue Provision Policy Statement

Where the Authority finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP). Although there has been no statutory minimum provision requirement since 2008, The Local Government Act 2003 requires the Authority to have regard to the MHCLG *Guidance on Minimum Revenue Provision* updated in 2018.

The broad aim of the MHCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The MHCLG Guidance requires the Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The following statement only incorporates options recommended in the Guidance.

For capital expenditure incurred before 1st April 2008, MRP will be determined in accordance with the former regulations that applied on 31st March 2008, incorporating an “Adjustment A” of £2.9m on a reducing balance method

For capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant assets in equal instalments, but under exceptional circumstances MRP the annuity or equal instalments method may apply. Furthermore, where appropriate provision of MRP will commence in the year after the asset becomes operational.

Estimated life periods will be determined under delegated powers. The Council may defer to the estimated useful economic life periods specified in the MRP guidance, but reserves the right to determine such periods and prudent MRP.
As some types of capital expenditure incurred by the Authority are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main

component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

For assets acquired by finance leases or the Private Finance Initiative, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

No MRP will be charged in respect of assets held within the Housing Revenue Account.

Third party loans – Under statutory requirements the payment of the loan will normally be treated as capital expenditure. The subsequent loan repayments, (which are treated as capital receipts under statutory requirements), will be used to reduce the long term liability and consequently the CFR. As a result MRP will not generally be charged on the loan as it is not appropriate to do so.

Agenda Item 9

Havering
LONDON BOROUGH

AUDIT COMMITTEE

Subject Heading:	Governance and Risk Update
SLT Lead:	Jane West Chief Operating Officer
Report Author and contact details:	Jeremy Welburn Head of Assurance. Tel: 01708 432610 / 07976539248 E-mail: jeremy.welburn@onesource.co.uk
Policy context:	To inform the Committee of progress against significant governance issues (as reported in the 2018/19 Annual Governance Statement) and an update on Risk Management.
Financial summary:	There are none arising directly from this report which is for noting and/or providing an opportunity for questions to be raised.

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[X]
Places making Havering	[X]
Opportunities making Havering	[X]
Connections making Havering	[X]

SUMMARY

This report advises the Committee on the progress against significant governance issues as reported in the 2018/19 Annual Governance Statement (AGS) and updates on Risk Management.

RECOMMENDATIONS

1. To note the contents of the report.

2. To raise any issues of concern and ask specific questions of officers where required.

REPORT DETAIL

1. Risk Management Update

1.1 A revised draft Risk Management Strategy was presented to Audit Committee in April 2019 along with an outline of areas of improvement, as identified in a review by Zurich.

1.2 A risk identification and horizon scanning session was held at the Governance and Assurance Board (GAB) and a training session has also been held with CLT members.

1.3 Progress has been made on developing the directorate risk registers with a risk workshop held with the Regeneration senior management team and an initial workshop held with Adults. Some work has been undertaken with Housing on their compliance risks with wider discussions on the Directorate risk register expected to commence in January 2020. A directorate risk register is now in place for the Chief Operating Officer (COO).

1.4 Workshops with Children's Services and Public Health are expected to be scheduled to take place in February 2020.

1.5 A draft Corporate Risk Register comprising of fourteen risks has been agreed by GAB and will be presented at an SLT meeting in January 2019. A revised Corporate Risk Register is expected to be presented at the next Audit Committee meeting in April 2020.

1.6 Risk Management continues to be co-ordinated by the Audit Manager.

2. Governance Update

2.1 Regulation 6(1b) of the Accounts and Audit Regulations 2015 requires all relevant bodies to prepare an Annual Governance Statement (AGS). The purpose of the AGS is to communicate to stakeholders the standards of corporate governance the organisation demonstrates and identify any significant issues that have arisen in year, and what is planned to address these issues. The Council has an officer Governance and Assurance Board which meets at least quarterly and is made up of the following standing members:

- Chief Operating Officer (S151 and Chair)
- Head of Assurance, oneSource
- Monitoring Officer (Deputy Director of Legal & Governance oneSource)
- Director of Finance (oneSource)
- Head of Finance (Strategic)
- Head of Procurement (oneSource)
- Head of the Programme Office
- Director of Human Resources / Organisational Development (oneSource)
- Assistant Director Transformation (customer representative)
- Technical Services Director (customer representative)
- Head of the Joint Commissioning Unit (customer representative)

2.2 This group oversees the process to produce the AGS annually and as a standing meeting item monitors and updates the action plan to address significant governance issues raised. The group maintains a record of new issues raised during the year and a detailed action plan to capture outcomes and achievements. Actions are allocated to responsible officers for progression between meetings.

2.3 The Governance Group is non-decision making and escalates issues to Senior Leadership Team. The output informs the Annual Governance Statement, Corporate Risk Register and other policies and procedures etc. as appropriate.

3. Annual Governance Statement (AGS) 2018/19 – action taken in relation to significant governance issues

3.1 The 2018/19 AGS was reported to the April 2019 Audit Committee.

3.2 The significant issues raised in the 2018/19 Annual Governance Statement are set out in detail in Appendix A and progress against each of these is reported there. For members' ease of reference the three areas identified are:

- Delivery of a balanced budget
- Embedding the governance culture and framework within the organisation; and
- EU Exit; preparations and impact.

Appendices: Provide supporting detail for Members' information

Appendix A: Governance and Assurance Board AGS 2018/19 Significant Issues Action Plan updated December 2019.

IMPLICATIONS AND RISKS

Financial implications and risks:

There are none arising directly from this report which is for noting and/or providing an opportunity for questions to be raised.

However, it should be noted that failure to appropriately manage risk could result in significant financial loss for the Council. Regular review and monitoring of the significant issues action plan will help to mitigate against this possibility. Failure to comply with best practice may lead to the Council not being viewed as open and transparent by stakeholders.

Legal implications and risks:

The Council is responsible for ensuring that it has a sound system of internal control which facilitates the effective exercise of its functions and the achievement of its aims and objectives, ensures that the financial and operational management of the authority is effective and includes effective arrangements for the management of risk (Regulation 3 of the Accounts and Audit Regulations 2015).
The Council must carry out an annual review of the effectiveness of its system of internal control which must be considered by the relevant committee. In the light of that review, the Council must produce an annual governance statement which must be approved by the relevant committee in advance of the Authority approving the statement of accounts (Regulations 6 (1), (2) and (4) of the Accounts and Audit Regulations 2015.

There are no apparent risks in noting the content of this report.

Human Resources implications and risks:

None arising directly from this report.

Equalities implications and risks:

None arising directly from this report. Equality and social inclusion are key factors to consider in the Council's governance arrangements and any changes to the Code of Governance or other related policies and procedures are assessed in order to ensure the impact is appropriately identified.

1. Delivery of a balanced budget: The Council was able to set a balance budget for the 2019/20 financial year. As set out in the report to Council there continues to be continued pressures over the medium term to the Council due to increased service demand and pressures while available resources are reducing. The continued financial landscape for the Council isn't set to change over the medium term and will continue to present challenges to the Council in setting a balance budgets for 2019/20 and beyond. Uncertainty around many aspects of the future funding model for Local Government remains a challenge in the medium term.	
Action Already Taken	**Planned Actions for 2019/20 and Progress**
• At the end of 2018/19 the Council was able to achieve a balance budget for 19/20. • The development of the 2019/20 budget and MTFS has fully taken account of the financial position being reported for 2018/19. At budget setting, the period 8 (30th November) monitoring report reviewed by Overview and Scrutiny Committee reported an overspend across Council service departments of £2.787m for 2018/19. The Senior Leadership Team has continued to focus on measures to contain expenditure within the approved budget in order to ensure financial stability as a basis for the 2019/20 budget and beyond. Work continued in year to reduce the overspend by the year end. • Officers reported to the Senior Leadership Team on a monthly basis from period 2 – 12 the anticipated outturn for the financial year, which identified medium term financial pressures and opportunities, and demonstrated management action to contain the in year position. • The Medium Term Financial Strategy, sets out the Council's financial forecast for the coming five years, aligned to the Corporate Plan, and will continue to monitor the anticipated levels of expenditure and income to the Council and the requirement for officers to identify efficiency opportunities. • The Council established a wider transformation and modernisation programme supporting the delivery of efficiencies whilst improving outcomes to residents and delivering the Council's corporate plan. • A corporate capital strategy was developed in line with the revised code of practice and this was approved with the capital programme alongside the MTFS report. This incorporated the work of the council's regeneration programmes.	Officers will continue to report to the Senior Leadership Team on a monthly basis from period 2 – 12 the anticipated outturn for the financial year, which will identified medium term financial pressures and opportunities. • The Medium Term Financial Strategy will continue to be updated and the corporate work plan is beginning from April to consider the budget challenge for the next year and medium term. Cabinet will receive updates on the MTFS and overarching financial position throughout the year. • The Council continues to deliver the transformation and modernisation programme, including the transition to Oracle Fusion. The theme boards will focus on the delivery of the transformation and core business. • Officers will continue to work with the administration to ensure that the financial challenge is clearly understood and they work collaboratively to support officers in identifying new opportunities to reduce the financial pressures facing the Council.
Lead Officer	**Target Date for Completion**
Jane West, Chief Operating Officer	March 2020

<table>
<tr><td colspan="2">2. Embedding the Governance Culture and Framework within the organisation: Further work needs to be undertaken to develop a comprehensive, auditable and objective assurance process to give reassurance that the Governance framework is understood and embedded within the organisation. Particular emphasis should be given to ensuring that any change in the governance framework is known and addressed and that new personnel are equipped with the correct knowledge and understanding.</td></tr>
<tr><td>Action Already Taken</td><td>Planned Actions for 2019/20 and Progress</td></tr>
<tr><td>Governance issues picked up within some individual audits during completion of the 2018/19 Internal Audit plan and recommendations raised to address them. Recommendations are followed up by Internal Audit and progressed monitored.
Ongoing compliance work as part of the Internal Audit Plan.
Governance Framework changes discussed and agreed as part of the work of the Governance and Assurance Board.</td><td>Highlighting of key governance changes.
Review and development of induction process.
Development of co-ordinated and monitored training programme.
Further specific governance and risk work allocated in the 2019/20 Internal Audit Plan - underway.
Oracle Fusion implementation underway (expected completion June 2020)
Remainder of compliance work in Internal Audit Plan</td></tr>
<tr><td>Lead Officer</td><td>Target Date for Completion</td></tr>
<tr><td>Jane West, Chief Operating Officer</td><td>March 2020</td></tr>
</table>

3. EU Exit: Preparations and Impact	
Action Already Taken	**Planned Actions for 2019/20 and Progress**
• Established a Corporate EU Exit Group, reporting weekly to SLT • Active participation in Borough, London and National related groups, e.g. London Resilience • Completion of the London Resilience Risk Register for Havering • Review of Borough Emergency Plan and arrangements against National standards • Training of Local Authority GOLD Officers • Updated BCPs • Testing of Borough Emergency Plan • Attendance at national events • Implemented weekly PI monitoring • Weekly returns to London Councils made • Weekly telephone conference with London Resilience/London Council Groups • Sign-posting of National Guidance (Community and Staff)	• Updates provided to MHCLG as required in the run up to 31 March 2019 • Review key Risk Mitigations • Support for LAC EU settlement status • MHCLG have recently stood down the requirement for central reporting in relation to Brexit
Lead Officer	**Target Date for Completion**
Jane West, Chief Operating Officer	March 2020

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Havering LONDON BOROUGH

AUDIT COMMITTEE

Subject Heading:	Accounting Policies 2019/20 & 2020/21
SLT Lead:	Jane West
Report Author and contact details:	Contact: Kevin Miles Designation: Financial Reporting Accountant Telephone: 01708 434551 E-mail address: kevin.miles@oneSource.co.uk
Policy context:	This report advises the Audit Committee of amendments required to the accounting policies adopted for preparation of the accounts for the financial year 2019/20 and 2020/21
Financial summary:	There are no direct financial implications to the report

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[]
Places making Havering	[]
Opportunities making Havering	[X]
Connections making Havering	[]

SUMMARY

This report summarises the main contents of the accounting policies adopted by the Council and the required changes to ensure the accounts for 2019/20 are prepared in accordance with accounting regulations. Any further changes to accounting regulations may require the policies to be changed further, however none are anticipated at this stage. Any significant changes to the 2019/20 policies will be highlighted to the committee in the Statement of Accounts report in July 2020.

- The report presents the accounting policies applicable to the financial year 2019/20 and will be reflected in the published statement of accounts. These policies will also provide the basis for the 2020/21 policies. At this stage there are no changes for 2020/21 identified other than the Leasing Standard IFRS 16 will have been adopted by Local Government – this will bring leased assets worth over £5,000 onto the balance sheet where the lease period exceeds one year.

- The CIPFA Better Governance Forum has produced a tool-kit for local authority Audit Committees that recommends Members review accounting policies on an annual basis. Adoption of the 2020/21 policies also means draft policies are in place for the start of the financial year to which they relate.

Appendix A includes the revised accounting policies for 2019/20 and 2020/21 combined into one document – differences are highlighted. The policies for both years are the same except where marked for leased assets and the changes to policy section. Relevant dates will be updated for the 2020/21 policies.

RECOMMENDATIONS

The Committee is asked to note and invited to comment on the accounting policies applicable to financial year 2019/20 and 2020/21.

REPORT DETAIL

1. Introduction

1.1 This report sets out the revised accounting policies that will be applied during the financial years 2019/20 and 2020/21 in preparation of the Council's financial statements. The full policies are shown in appendix A to this report and will be included in the Statement of Accounts. The policies are prepared under the International Financial Reporting Standards (IFRS). Members of the Audit Committee are invited to note these policies and make comment. Reviewing of accounting policies by Members ensures that the Council and Audit Committee follow the CIPFA Better Governance Forum toolkit for local authority Audit Committees.

1.2 Unless there are major changes to accounting rules and regulation, accounting policies do not change significantly between years because the accounts would not be comparable from one year to the next.

1.3 The audited Statement of Accounts for 2019/20 will be presented to the July 2020 Audit Committee for approval. The accounting policies statement will be included within the accounts and any changes made during the course of the closedown programme and/or audit will be highlighted and explained by officers.

2. Purpose of Accounting Policies

2.1 The Code of Practice for Local Authority Accounting defines accounting policies as "the principles, bases, conventions, rules and practices applied by an authority that specify how the effects of transactions and other events are to be reflected in its financial statements through recognising, selecting measurement bases for, and presenting assets, liabilities, gains, losses and changes in reserves".

2.2 The application of accounting policies supports the implementation of the main accounting concepts of best practice. These ensure financial reports:

- Are **relevant** – providing appropriate information on the stewardship of Authority monies.
- Are **reliable** – financial information can be relied upon and is without bias and free from error, within the bounds of materiality and has been prudently prepared.
- Allow **comparability** – the interpretation of financial reports is enhanced by being able to compare information across other accounting periods and other organisations.
- Are **understandable** – though financial reports have to contain certain information, they have to be understandable.
- Reflect **material** informatio**n** – significant transactions must be incorporated in the financial reports.
- Prepared on a **going concern** basis – the assumption that the authority will continue in operational existence for the foreseeable future.
- Prepared on an **accruals** basis – accounts are prepared to reflect the benefit of goods and services received and provided rather than when cash transactions occur when invoices are paid in a later accounting period.

2.3 The accounting policies currently adopted by the Council are in line with the concepts set out in 2.2.

3. Contents of Accounting Policies

3.1 The appendix contains all of the Council's accounting policies. The more significant policies cover the treatment of the following:

- **Property Plant and Equipment** – the basis for valuing major long-term assets, such as council dwellings and offices.
- **Impairment** – The carrying value of assets is reviewed annually to determine whether there is a material change in value and the basis on which impairment losses are written off.
- **Depreciation** – Depreciation is charged to spread the value of an asset over its useful life.
- **Provisions and reserves** – A **provision** is created because the Council will have to make a future payment to settle a financial obligation and a

reasonable estimate can be made of the amount payable. Provisions are charged to the relevant service area. A **reserve** is created for a planned future purpose or maintained as a general contingency. These are recorded separately on the Movement in Reserves Statement.

- **Accruals of Income and Expenditure** – The Council raises accruals to comply with the concept of accounting to measure when payments or receipts are due rather than where cash is transferred to settle the liability
- **Pensions** – This note describes the three pension schemes Council employees contribute to (teachers, health workers and Local Government Pension Scheme). The policy includes detail on the investment valuation basis used and the calculations made of future liability.
- **Value Added Tax** - As the vast majority of VAT paid by the Council is recoverable from H.M. Revenue & Customs, recoverable VAT is excluded from the cost of services within the accounts.

4. Changes in Accounting Policies for 2019/20

4.1 The application of most accounting policies is applied consistently from year to year. Changes are required when new accounting regulations are introduced or updated or if there is a significant change within the financial activities of the Council.

4.2 There are no material changes proposed to Havering's accounting policies for the 2019/20 accounts.

5 Changes in Accounting Policies for 2020/21

No material changes to the 2020/21 policies are expected other than the requirement to bring all leased in assets worth over £5,000 onto the balance sheet from 1 April 2021. Officers are working to identify all leased assets and will agree the proposed accounting treatment with EY prior to the 2020/21 closedown. This change in accounting treatment should not have a material impact upon the Council's usable financial resources.

IMPLICATIONS AND RISKS

Financial implications and risks:

There are no direct financial implications arising from the publication or approval of accounting policies. There are no material changes to policy impacting upon the Councils financial position.

Legal implications and risks:

There are no apparent legal implications in noting the content of the Report.

Human Resources implications and risks:

no implications

Equalities implications and risks:

no implications

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Notes to the Core Financial Statements

1. Accounting Policies

Going Concern

The concept of a going concern assumes that an authority, its functions and services will continue in operational existence for the foreseeable future. Where this is not the case, particular care will be needed in the valuation of assets, as inventories and property, plant and equipment may not be realisable at their book values and provisions may be needed for closure costs or redundancies. An inability to apply the going concern concept can have a fundamental impact on the financial statements.

Accounts drawn up under the Code assume that a local authority's services will continue to operate for the foreseeable future. This assumption is made because local authorities carry out functions essential to the local community and are themselves revenue-raising bodies (with limits on their revenue-raising powers arising only at the discretion of Central Government). If an authority was in financial difficulty, the prospects are thus that alternative arrangements might be made by Central Government either for the continuation of the services it provides or for assistance with the recovery of a deficit over more than one financial year.

i. General Principles

The Statement of Accounts summarises the Authority's transactions for the 2019/20 financial year and its position at the year end of 31 March 2020. The Authority is required to prepare an annual Statement of Accounts by 31 May 2020, which the Accounts and Audit (England) Regulations 2015 require to be prepared in accordance with proper accounting practices. These practices primarily comprise the *Code of Practice on Local Authority Accounting in the United Kingdom 2019/20*, supported by International Financial Reporting Standards (IFRS) and statutory guidance issued under section 12 of the Local Government Act 2003.

The accounting convention adopted in the Statement of Accounts is principally historical cost, modified by the revaluation of certain categories of non-current assets and financial instruments.

ii. Accruals of Income and Expenditure

Activity is accounted for in the year that it takes place, not simply when cash payments are made or received. In particular:

- Revenue from contracts with service recipients, whether for services or the provision of goods, is recognised when (or as) the goods or services are transferred to the service recipient in accordance with the performance obligations in the contract.

- supplies are recorded as expenditure when they are consumed – where there is a gap between the date supplies are received and their consumption, they are carried as inventories on the Balance Sheet;

- expenses in relation to services received (including services provided by employees) are recorded as expenditure when the services are received rather than when payments are made. Outstanding creditors are written out of the accounts if they have not been billed for by the supplier after a period of one year, however a sample of outstanding balances will be sampled and adjusted for if required;

- interest receivable on investments and payable on borrowings is accounted for respectively as income and expenditure on the basis of the effective interest rate for the relevant financial instrument rather than the cash flows fixed or determined by the contract.
- where revenue and expenditure have been recognised but cash has not been received or paid, a debtor or creditor for the relevant amount is recorded in the Balance Sheet. Where debts may not be settled, the balance of debtors is written down and a charge made to revenue for the income that might not be collected; and
- most accruals are automatically generated by the feeder system concerned, but a de minimis is applied in respect of accruals raised manually unless material to grant funding streams or to individual budgets. The de minimis for 2019/20 remains at £50,000.

iii. Cash and Cash Equivalents

Cash is represented by cash in hand and deposits with financial institutions, repayable without penalty on notice of not more than 24 hours. Cash equivalents are highly liquid investments that mature in one month or less from the date of acquisition or notice accounts of no more than 3 months and that are readily convertible to known amounts of cash with insignificant risk of change in value.

In the Cash Flow Statement, cash and cash equivalents are shown net of bank overdrafts that are repayable on demand and form an integral part of the Authority's cash management.

iv. Prior Period Adjustments, Changes in Accounting Policies and Estimates and Errors

Prior period adjustments may arise as a result of a change in accounting policies or to correct a material error. Changes in accounting estimates are accounted for prospectively, i.e. in the current and future years affected by the change and do not give rise to a prior period adjustment.

Changes in accounting policies are only made when required by proper accounting practices or the change provides more reliable or relevant information about the effect of transactions, other events and conditions on the Authority's financial position or financial performance. Where a change is made, it is applied retrospectively (unless stated otherwise) by adjusting opening balances and comparative amounts for the prior period as if the new policy had always been applied. Material errors discovered in prior period figures are corrected retrospectively by amending opening balances and comparative amounts for the prior period.

Within the accounts the Comprehensive Income and Expenditure Statement has been restated to comply with the CIPFA code; 'Telling the story'. This is to improve the presentation and transparency of the Council's financial statements.

v. Charges to Revenue for Non-Current Assets

Services are debited with the following amounts to record the cost of holding fixed assets during the year:

- depreciation attributable to the assets used by the relevant service;
- revaluation and impairment losses on assets used by the service where there are no accumulated gains in the Revaluation Reserve against which the losses can be written off; and
- amortisation of intangible non-current assets attributable to the service.

The Authority is not required to raise council tax to fund depreciation, revaluation and impairment losses or amortisations. However, it is required to make an annual contribution from revenue towards the reduction in its overall borrowing requirement equal to an amount calculated on a prudent basis determined by the Authority in accordance with statutory guidance (the Minimum Revenue Provision). Depreciation, revaluation and impairment losses, and amortisations are therefore replaced by an adjusting transfer to the General Fund Balance from the Capital Adjustment Account in the Movement in Reserves Statement for the difference between the two.

vi. Council Tax and Non-Domestic Rates

Billing authorities act as agents, collecting council tax and non-domestic rates (NDR) on behalf of the major preceptors (including Central Government for NDR) and, as principals, collecting council tax and NDR for themselves. Billing authorities are required by statute to maintain a separate fund (i.e. the Collection Fund) for the collection and distribution of amounts due in respect of council tax and NDR. Under the legislative framework for the Collection Fund, billing authorities, major preceptors and Central Government share proportionately the risks and rewards that the amount of council tax and NDR collected could be less or more than predicted.

Accounting for Council Tax and NDR

The council tax and NDR income included in the Comprehensive Income and Expenditure Statement is the Authority's share of accrued income for the year. However, regulations determine the amount of council tax and NDR that must be included in the authority's General Fund. Therefore, the difference between the income included in the Comprehensive Income and Expenditure Statement and the amount required by regulation to be credited to the General Fund is taken to the Collection Fund Adjustment Account and included as a reconciling item in the Movement in Reserves Statement.

The Balance Sheet includes the Authority's share of the end of year balances in respect of council tax and NDR relating to arrears, impairment allowances for doubtful debts, overpayments and prepayments and appeals. Where debtor balances for the above are identified as impaired because of a likelihood arising from a past event that payments due under the statutory arrangements will not be made (fixed or determinable payments), the asset is written down and a charge made to the Financing and Investment Income and Expenditure line in the CIES. The impairment loss is measured as the difference between the carrying amount and the revised future cash flows.

vii. Employee Benefits

Benefits Payable During Employment

Short-term employee benefits are those due to be settled within 12 months of the year end. They include such benefits as salaries, paid annual leave and paid sick leave, bonuses and non-monetary benefits for current employees and are recognised as an expense for services in the year in which employees render service to the Authority. An accrual is made for the cost of holiday entitlements (or any form of leave, e.g. flexitime) earned by employees but not taken before the year end which employees can carry forward into the next financial year. The accrual is made at the salary rates applicable in the following accounting year, being the period in which the employee takes the benefit. The accrual is charged to Surplus or Deficit on the Provision of Services, but then reversed out through the Movement in Reserves Statement so that holiday benefits are charged to revenue in the financial year in which the holiday absence occurs.

Termination Benefits

Termination benefits are amounts payable as a result of a decision by the Authority to terminate an officer's employment before the normal retirement date, or an officer's decision to accept voluntary redundancy in exchange for those benefits. They are charged on an accruals basis to the relevant service line or, where applicable, to the Non Distributed Costs line in the Comprehensive Income and Expenditure Statement when the Authority can no longer withdraw the offer of those benefits or when the Authority recognises costs for a restructuring.

Where termination benefits involve the enhancement of pensions, statutory provisions require the General Fund and Housing Revenue Account balances to be charged with the amount payable by the Authority to the Pension Fund or pensioner in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, appropriations are required to and from the Pensions Reserve to remove the notional debits and credits for pension enhancement termination benefits and replace them with debits for the cash paid to the Pension Fund and pensioners and any such amounts payable but unpaid at the year end.

Post-Employment Benefits

Employees of the Authority are members of three separate pension schemes:

- the Teachers' Pension Scheme, administered by Capita Teachers' Pensions on behalf of the Department for Education (DfE);
- the National Health Service Pension Scheme, administered by the National Health Service; and
- the Local Government Pension Scheme, administered by the Authority.

All three schemes provide defined benefits to members (retirement lump sums and pensions), earned as employees work for the Authority. However, the arrangements for the Teachers' and National Health Service schemes mean that liabilities for these benefits cannot ordinarily be identified specifically to the Authority. Those schemes are therefore accounted for as if they were defined contribution scheme and no liability for future payments of benefits is recognised in the Balance Sheet. The Children's and Education and Public Health Services lines in the Comprehensive Income and Expenditure Statement are charged with the employer's contributions payable to the Teachers' and National Health Service Pensions Scheme in the year.

The Local Government Pension Scheme

The Local Government Scheme is accounted for as a defined benefits scheme.

- The liabilities of the London Borough of Havering Pension Fund attributable to the Authority are included in the Balance Sheet on an actuarial basis using the projected unit method – i.e. an assessment of the future payments that will be made in relation to retirement benefits earned to date by employees, based on assumptions about mortality rates, employee turnover rates, etc., and projections of projected earnings for current employees
- Liabilities are discounted to their value at current prices, using a discount rate of 4.5% based on the indicative rate of return on high quality corporate bonds.
- The assets of the London Borough of Havering Pension Fund attributable to the Authority are included in the Balance Sheet at their fair value:
    - quoted securities – current bid price;
    - unquoted securities – professional estimate;
    - unitised securities – current bid price; and
    - property – market value.

The change in the net pension liability is analysed into the following components:

- Service cost comprising:

  - current service cost – the increase in liabilities as a result of years of service earned this year – allocated in the Comprehensive Income and Expenditure Statement to the services for which the employees worked
  - past service cost – the increase in liabilities as a result of a scheme amendment or curtailment whose effect relates to years of service earned in earlier years – debited to the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement as part of Non Distributed Costs
  - net interest on the net defined benefit liability (asset), i.e. net interest expense for the Authority – the change during the period in the net defined benefit liability (asset) that arises from the passage of time charged to the Financing and Investment Income and Expenditure line of the Comprehensive Income and Expenditure Statement – this is calculated by applying the discount rate used to measure the defined benefit obligation at the beginning of the period to the net defined benefit liability (asset) at the beginning of the period – taking into account any changes in the net defined benefit liability (asset) during the period as a result of contribution and benefit payments.

- Re-measurements comprising:
  - the return on plan assets – excluding amounts included in net interest on the net defined benefit liability (asset) – charged to the Pensions Reserve as other comprehensive income and expenditure;
  - actuarial gains and losses – changes in the net pensions liability that arise because events have not coincided with assumptions made at the last actuarial valuation or because the actuaries have updated their assumptions – charged to the Pensions Reserve as other comprehensive income and expenditure;
  - contributions paid to the London Borough of Havering pension fund – cash paid as employer's contributions to the pension fund in settlement of liabilities; not accounted for as an expense.

In relation to retirement benefits, statutory provisions require the General Fund Balance to be charged with the amount payable by the Authority to the Pension Fund or directly to pensioners in the year, not the amount calculated according to the relevant accounting standards. In the Movement in Reserves Statement, this means that there are appropriations to and from the Pensions Reserve to remove the notional debits and credits for retirement benefits and replace them with debits for the cash paid to the Pension Fund and pensioners and any such amounts payable but unpaid at the year end. The negative balance that arises on the Pensions Reserve thereby measures the beneficial impact to the General Fund of being required to account for retirement benefits on the basis of cash flows rather than as benefits are earned by employees.

Discretionary Benefits

The Authority also has restricted powers to make discretionary awards of retirement benefits in the event of early retirements. Any liabilities estimated to arise as a result of an award to any member of staff (including teachers) are accrued in the year of the decision to make the award and accounted for using the same policies as are applied to the Local Government Pension Scheme.

viii. Events After the Reporting Period

Events after the Balance Sheet date are those events, both favourable and unfavourable, that occur between the end of the reporting period and the date when the Statement of Accounts is authorised for issue. Two types of events can be identified:

- those that provide evidence of conditions that existed at the end of the reporting period – the Statement of Accounts is adjusted to reflect such events; and
- those that are indicative of conditions that arose after the reporting period – the Statement of Accounts are not adjusted to reflect such events, but where a category of events would have a material effect, disclosure is made in the notes of the nature of the events and their estimated financial effect.

Events taking place after the date of authorisation for issue are not reflected in the Statement of Accounts.

ix. Financial Instruments

Financial Liabilities

Financial liabilities are recognised on the Balance Sheet when the Authority becomes a party to the contractual provisions of a financial instrument and are initially measured at fair value and are carried at their amortised cost. Annual charges to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement for interest payable are based on the carrying amount of the liability, multiplied by the effective rate of interest for the instrument. The effective interest rate is the rate that exactly discounts estimated future cash payments over the life of the instrument to the amount at which it was originally recognised.

For most of the borrowings that the Authority has, this means that the amount presented in the Balance Sheet is the outstanding principal repayable (plus accrued interest); and interest charged to the Comprehensive Income and Expenditure Statement is the amount payable for the year according to the loan agreement.

Gains and losses on the repurchase or early settlement of borrowing are credited and debited to the Comprehensive Income and Expenditure Statement in the year of repurchase/settlement. However, where repurchase has taken place as part of a restructuring of the loan portfolio that involves the modification or exchange of existing instruments, the premium or discount is respectively deducted from or added to the amortised cost of the new or modified loan and the write-down to the Comprehensive Income and Expenditure Statement is spread over the life of the loan by an adjustment to the effective interest rate.

Where premiums and discounts have been charged to the Comprehensive Income and Expenditure Statement, regulations allow the impact on the General Fund Balance to be spread over future years. The Authority has a policy of spreading the gain or loss over the term that was remaining on the loan against which the premium was payable or discount receivable when it was repaid. The reconciliation of amounts charged to the Comprehensive Income and Expenditure Statement to the net charge required against the General Fund Balance is managed by a transfer to or from the Financial Instruments Adjustment Account in the Movement in Reserves Statement.

Financial Assets

Financial assets are classified based on a classification and measurement approach that reflects the business model for holding the financial assets and their cashflow characteristics. There are three main classes of financial assets measured at:

- amortised cost
- fair value through profit or loss (FVPL), and
- fair value through other comprehensive income (FVOCI)

The authority's business model is to hold investments to collect contractual cash flows. Financial assets are therefore classified as amortised cost, except for those whose contractual payments are not solely payment of principal and interest (i.e. where the cash flows do not take the form of a basic debt instrument).

Financial Assets Measured at Amortised Cost

Financial assets measured at amortised cost are recognised on the Balance Sheet when the authority becomes a party to the contractual provisions of a financial instrument and are initially measured at fair value. They are subsequently measured at their amortised cost. Annual credits to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement (CIES) for interest receivable are based on the carrying amount of the asset multiplied by the effective rate of interest for Statements the instrument. For most of the financial assets held by the authority, this means that the amount presented in the Balance Sheet is the outstanding principal receivable (plus accrued interest) and interest credited to the CIES is the amount receivable for the year in the loan agreement.

Any gains and losses that arise on the de-recognition of an asset are credited or debited to the Financing and Investment Income and Expenditure line in the CIES.

Expected Credit Loss Model

The authority recognises expected credit losses on all of its financial assets held at amortised cost [or where relevant FVOCI], either on a 12-month or lifetime basis. The expected credit loss model also applies to lease receivables and contract assets. Only lifetime losses are recognised for trade receivables (debtors) held by the authority.

Impairment losses are calculated to reflect the expectation that the future cash flows might not take place because the borrower could default on their obligations. Credit risk plays a crucial part in assessing losses. Where risk has increased significantly since an instrument was initially recognised, losses are assessed on a lifetime basis. Where risk has not increased significantly or remains low, losses are assessed on the basis of 12-month expected losses.

Financial Assets Measured at Fair Value through Profit of Loss (FVPL)

Financial assets that are measured at FVPL are recognised on the Balance Sheet when the authority becomes a party to the contractual provisions of a financial instrument and are initially measured and carried at fair value. Fair value gains and losses are recognised as they arrive in the Surplus or Deficit on the Provision of Services.

The fair value measurements of the financial assets are based on the following techniques:

- instruments with quoted market prices – the market price
- other instruments with fixed and determinable payments – discounted cash flow analysis.

The inputs to the measurement techniques are categorised in accordance with the following three levels:

- Level 1 inputs – quoted prices (unadjusted) in active markets for identical assets that the authority can access at the measurement date.
- Level 2 inputs – inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly.
- Level 3 inputs – unobservable inputs for the asset. Any gains and losses that arise on the de-recognition of the asset are credited or debited to the Financing and Investment Income and Expenditure line in the Comprehensive

x. Foreign Currency Translation

Where the Authority has entered into a transaction denominated in a foreign currency, the transaction is converted into sterling at the exchange rate applicable on the date the transaction was effective. Where amounts in foreign currency are outstanding at the year end, they are reconverted at the spot exchange rate at 31 March. Resulting gains or losses are recognised in the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement.

xi. Government Grants and Contributions

Whether paid on account, by instalments or in arrears, government grants and third party contributions and donations are recognised as due to the Authority when there is reasonable assurance that:

- the Authority will comply with the conditions attached to the payments; and
- the grants or contributions will be received.

Amounts recognised as due to the Authority are not credited to the Comprehensive Income and Expenditure Statement until conditions attached to the grant or contribution have been satisfied. Conditions are stipulations that specify that the future economic benefits or service potential embodied in the asset in the form of the grant or contribution are required to be consumed by the recipient as specified, or future economic benefits or service potential must be returned to the transferor.

Monies advanced as grants and contributions for which conditions have not been satisfied are carried in the Balance Sheet as creditors. When conditions are satisfied, the grant or contribution is credited to the relevant service line (attributable revenue grants and contributions) or Taxation and Non-Specific Grant Income (non ring-fenced revenue grants and all capital grants) in the Comprehensive Income and Expenditure Statement.

All Town and Country Planning Act 1990 (as amended) Section 106 contributions, because of their complex nature and numerous legal conditions, are only recognised through the Comprehensive Income and Expenditure Statement once they have been spent. Only then are we certain all conditions have been met and there is no return obligation.

Where capital grants are credited to the Comprehensive Income and Expenditure Statement, they are reversed out of the General Fund and Housing Revenue Account balances in the Movement in Reserves Statement. Where the grant has yet to be used to finance capital expenditure, it is posted to the Capital Grants Unapplied Reserve. Where it has been applied, it is posted to the Capital Adjustment Account. Amounts in the Capital Grants Unapplied Reserve are transferred to the Capital Adjustment Account once they have been applied to fund capital expenditure.

Non Ring-fenced Grants

These are allocated by Central Government directly to local authorities as additional revenue funding. They are not ring-fenced and are credited to the Taxation and Non-Specific Grant Income in the Comprehensive Income and Expenditure Statement.

Business Improvement Districts

The Authority is the billing authority for the London Riverside Business Improvement District (BID) managed by Ferry Lane Action Group, which provides a cleaner, safer, more secure business environment and promotes the interests of the business community within the BID. The Authority acts as principal under the scheme, and accounts for income received and expenditure incurred (including contributions to the BID project) on the balance sheet. The Authority has similar arrangements for the Romford Town Centre BID, which went live during 2018/19.

xii. Heritage Assets

The Authority's Heritage Assets are split into two categories

- Civic Regalia; and
- Heritage Buildings.

Civic Regalia

The collection of civic regalia includes the Mayor's and the Deputy Mayor's chains, which are worn on ceremonial duties and various items with civic insignia. They are valued based on manufacturing costs and do not include any element for rarity or collectable value, retail mark-up or VAT.

Heritage Buildings

The Authority owns one building that meets the definition of a heritage asset and this is Upminster Windmill. The building has been valued by professional valuers who have stated that the most appropriate means of valuing this building is by its historic cost.

The carrying amounts of heritage assets are reviewed where there is evidence of impairment for heritage assets, e.g. where an item has suffered physical deterioration or breakage or where doubts arise as to its authenticity. Any impairment is recognised and measured in accordance with the Authority's general policies on impairment.

xiii. Intangible Assets

Expenditure on non-monetary assets that do not have physical substance but are controlled by the Authority as a result of past events (e.g. software licences) is capitalised when it is expected that future economic benefits or service potential will flow from the intangible asset to the Authority.

Internally generated assets are capitalised where it is demonstrable that the project is technically feasible and is intended to be completed (with adequate resources being available) and the Authority will be able to generate future economic benefits or deliver service potential by being able to sell or use the asset. Expenditure is capitalised where it can be measured reliably as attributable to the asset and is restricted to that incurred during the development phase (research expenditure cannot be capitalised). Expenditure on the development of websites is not capitalised if the website is solely or primarily intended to promote or advertise the Authority's goods or services.

Intangible assets are measured initially at cost. Amounts are only revalued where the fair value of the assets held by the Authority can be determined by reference to an active market. In practice, no intangible asset held by the Authority meets this criterion, and they are therefore carried at amortised cost. The depreciable amount of an intangible asset is amortised over its useful life to the relevant service line(s) in the Comprehensive Income and Expenditure Statement. An asset is tested for impairment whenever there is an indication that the asset might be impaired – any losses recognised are posted to the relevant service line(s) in the Comprehensive Income and Expenditure Statement. Any gain or loss arising on the disposal or abandonment of an intangible asset is posted to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement.

Where expenditure on intangible assets qualifies as capital expenditure for statutory purposes, amortisation, impairment losses and disposal gains and losses are not permitted to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and (for any sale proceeds greater than £10,000) the Capital Receipts Reserve.

xiv. Inventories

The Authority has a small number of inventories. These are included in the Balance Sheet at the lower of cost and net realisable value. The cost of inventories is assigned predominantly using the first in first out (FIFO) costing formula.

xv. Investment Property

Investment properties are those that are used solely to earn rentals and/or for capital appreciation. The definition is not met if the property is used in any way to facilitate the delivery of services or production of goods or is held for sale.

Investment properties are measured initially at cost and subsequently at fair value, based on the amount at which the asset could be exchanged between knowledgeable parties at arm's length. Properties are not depreciated but are revalued annually according to market conditions at the year end. Gains and losses on revaluation are posted to the Financing and Investment Income and Expenditure line in the Comprehensive Income and Expenditure Statement. The same treatment is applied to gains and losses on disposal.

Rentals received in relation to investment properties are credited to the Financing and Investment Income line and result in a gain for the General Fund Balance. However, revaluation and disposal gains and losses are not permitted by statutory arrangements to have an impact on the General Fund Balance. The gains and losses are therefore reversed out of the General Fund Balance in the Movement in Reserves Statement and posted to the Capital Adjustment Account and (for any sale proceeds greater than £10,000) the Capital Receipts Reserve.

xvi. Interests in Companies and Other Entities

The code requires local authorities with, in aggregate, material interest in subsidiaries and associated companies and joint ventures to prepare group financial statements.

The Group's financial statement incorporate the financial statements of the London borough of Havering and its subsidiaries prepared as at the year end date. As part of the consolidation process, Havering has aligned the accounting policies of the subsidiaries with those of the Council and made consolidation adjustments where necessary; Consolidated the financial statements of the subsidiaries with those of the Council on a line by line basis; Eliminated in full balances, transactions, income and expenses between the Council and the partnerships.

xvii. Interest in Joint Committee

oneSource is a participative arrangement created by the Authority, the London Borough of Newham and the London Borough of Bexley to share back office operations. It is governed by a joint committee and is not deemed to meet the definition of joint control; hence the assets, liabilities, income, expenditure and cash flows of the joint committee are not consolidated into the Authority's group accounts. Instead, the Authority accounts for its own transactions arising within the agreement, including the assets, liabilities, income, expenditure and cash flows, in its single entity financial statements. Cost and savings are shared between the three authorities on the basis of an agreed formula and are allocated on an annual basis.

xviii. Leases (2019/20 Policy)

All current leases are classified as operating leases. Where a lease covers both land and buildings, the land and buildings elements are considered separately for classification. Arrangements that do not have the legal status of a lease, but convey a right to use an asset in return for payment, are accounted for under this policy where fulfilment of the arrangement is dependent on the use of specific assets.

The Authority as Lessee

Rentals paid under operating leases are charged to the Comprehensive Income and Expenditure Statement as an expense of the services benefitting from use of the leased property, plant or equipment. Charges are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a rent-free period at the commencement of the lease).

The Authority as Lessor

Where the Authority grants an operating lease over a property or an item of plant or equipment, the asset is retained on the Balance Sheet. Rental income is credited to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement. Credits are made on a straight-line basis over the life of the lease, even if this does not match the pattern of payments (e.g. there is a premium paid at the commencement of the lease). Initial direct costs incurred in negotiating and arranging the lease are added to the carrying amount of the relevant asset and charged as an expense over the lease term on the same basis as rental income.

Leases (2020/21 Revised Policy)

The Authority as Lessee

From 1 April 2021, where the Council is leasing an asset for more than 12 months and has a value in excess of £5,000, the asset will be accounted as if the asset was owned by the Council . Costs for assets Items under the deminimis level are recognised as revenue expenditure.

The initial recognition of the asset is at fair value of the property the Council has a right to use. A liability is also recognised which will reduce as lease payments are made.

The Authority as Lessor

Where the Council is the lessor for a lease, the asset is not recognised on the balance sheet, however a long term debtor at the present value of minimum lease payments is recognised. Income received is split between capital – credited against the debtor and finance income – credited to the Comprehensive Income and Expenditure Statement as interest receivable.

xix. Overheads and Support Services

The costs of overheads and support services are charged to those that benefit from the supply or service. The total absorption costing principle is used – the full cost of overheads and support services are shared between users in proportion to the benefits received

xx. Property, Plant and Equipment

Assets that have physical substance and are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes and that are expected to be used during more than one financial year are classified as Property, Plant and Equipment.

Recognition

Expenditure on the acquisition, creation or enhancement of Property, Plant and Equipment is capitalised on an accruals basis, provided that it is probable that the future economic benefits or service potential associated with the item will flow to the Authority and the cost of the item can be measured reliably. Expenditure that maintains but does not add to an asset's potential to deliver future economic benefits or service potential (i.e. repairs and maintenance) is charged as an expense when it is incurred.

Measurement

Assets are initially measured at cost, comprising:

- the purchase price
- any costs attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management
- the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located.

Finance costs are excluded in valuations for all assets.

Havering has applied the following de minimis criteria for the capitalisation of expenditure, so that schemes which cost less than this are classified as revenue rather than capital: -

• works to buildings	£5,000
• infrastructure	£5,000
• office and information technology	£5,000
• other furniture and equipment	£5,000

There are no de minimis limits for the following categories: land acquisition, vehicles and plant, energy conservation work, health and safety improvements, aids and adaptations for the disabled.

These de minimis rules may be waived where grant or borrowing consent is made available for items of capital expenditure below £5,000.

The cost of assets acquired other than by purchase is deemed to be its fair value, unless the acquisition does not have commercial substance (i.e. it will not lead to a variation in the cash flows of the Authority). In the latter case, where an asset is acquired via an exchange, the cost of the acquisition is the carrying amount of the asset given up by the Authority.

Assets are then carried in the Balance Sheet using the following measurement bases:

- infrastructure, community assets and assets under construction – depreciated historical cost;
- dwellings – current value, determined using the basis of existing use value for social housing (EUVSH);
- council offices – current value, determined as the amount that would be paid for the asset in its existing use (existing use value – EUV);
- school buildings – current value, but because of their specialist nature, are measured at depreciated replacement cost which is used as an estimate of current value;
- surplus assets – the current value measurement base is fair value, estimated at highest and best use from a market participant's perspective;
- all other assets – current value, determined as the amount that would be paid for the asset in its existing use (existing use value – EUV).

Where there is no market-based evidence of fair value because of the specialist nature of an asset, depreciated replacement cost (DRC) is used as an estimate of fair value. Where non-property assets that have short useful lives or low values (or both), depreciated historical cost basis is used as a proxy for fair value.

Assets included in the Balance Sheet at fair value are re-valued as a minimum every five years, with high value assets being re-valued annually, to ensure their carrying amount is not materially different from their fair value at the year end. In addition, an independent review is carried out annually. Increases in valuations are matched by credits to the Revaluation Reserve to recognise unrealised gains. (Exceptionally, gains might be credited to the Comprehensive Income and Expenditure Statement where they arise from the reversal of a loss previously charged to a service.)

Where decreases in value are identified, they are accounted for as follows:

- where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains); and
- where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the Comprehensive Income and Expenditure Statement.

The Revaluation Reserve contains revaluation gains recognised since 1 April 2007 only, the date of its formal implementation. Gains arising before that date have been consolidated into the Capital Adjustment Account.

Development Costs

General Feasibility studies are automatically treated as revenue, unless in very rare circumstances when they lead to the creation of an asset. This is because they are typically an options review of what schemes may or may not be considered for the capital programme. They do not in and of themselves produce an asset. There would need to be an accompanying business case justification as to why this expenditure could be capitalised and as such, this would normally only occur in relation to large-scale regeneration schemes.

The watershed moment between the feasibility and the development stage, when concrete designs are reviewed is normally the point at which expenditure may be considered for capitalisation. The Council's policy at this stage is to treat the expenditure as capital and then if the scheme did not go ahead or was stopped at an early stage without producing any assets, would treat the expenditure as an abortive revenue cost. This policy could be broadly described as *capitalising at risk* and all schemes that were cancelled without producing an asset would need to be reviewed for the potential for these abortive costs.

Impairment

Assets are assessed at each year end as to whether there is any indication that an asset may be impaired. Where indications exist and any possible differences are estimated to be material, the recoverable amount of the asset is estimated and, where this is less than the carrying amount of the asset, an impairment loss is recognised for the shortfall. Where impairment losses are identified, they are accounted for as follows:

- where there is a balance of revaluation gains for the asset in the Revaluation Reserve, the carrying amount of the asset is written down against that balance (up to the amount of the accumulated gains); and
- where there is no balance in the Revaluation Reserve or an insufficient balance, the carrying amount of the asset is written down against the relevant service line(s) in the Comprehensive Income and Expenditure Statement.

Where an impairment loss is reversed subsequently, the reversal is credited to the relevant service line(s) in the Comprehensive Income and Expenditure Statement, up to the amount of the original loss, adjusted for depreciation that would have been charged if the loss had not been recognised.

Depreciation

Depreciation is provided for on all property, plant and equipment by the systematic allocation of their depreciable amounts over their useful lives. An exception is made for assets without a determinable finite useful life (i.e. freehold land and certain community assets) and assets that are not yet available for use (i.e. assets under construction). Depreciation is not charged in the year of acquisition but is charged in full during the year of disposal.

Depreciation is calculated on the following bases:

- dwellings and other buildings – straight-line allocation over the useful life of the property as estimated by the valuer;
- vehicles, plant, furniture and equipment – straight-line allocation over a five year period unless a suitably qualified officer determines a more appropriate period; and
- infrastructure – straight-line allocation over 20 years.

Where an item of Property, Plant and Equipment has major components whose cost is significant in relation to the total cost of the item, the Code requires that these components are depreciated separately.

Major components which have materially different asset lives will be identified in respect of:

- new capital expenditure as it arises; and
- existing assets as they become subject to revaluation.

Assets will not be valued on a componentised basis in the following circumstances on the basis that the impact upon asset valuation and depreciation is not material to the accounting disclosures:

- capital expenditure of less than £300,000 per scheme; and
- assets valued at less than £3,000,000.

As a consequence of the application of this policy the Authority has not identified any major components with materially different asset lives. However, the application of this policy will be reviewed on an on-going basis to ensure that the carrying value of assets is not materially affected.

Revaluation gains are also depreciated, with an amount equal to the difference between current value depreciation charged on assets and the depreciation that would have been chargeable based on their historical cost being transferred each year from the Revaluation Reserve to the Capital Adjustment Account.

Disposals and Non-current Assets Held for Sale

When it becomes probable that the carrying amount of an asset will be recovered principally through a sale transaction rather than through its continuing use, it is reclassified as an Asset Held for Sale. The asset is revalued immediately before reclassification and then carried at the lower of this amount and fair value less costs to sell. Where there is a subsequent decrease to fair value less costs to sell, the loss is posted to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement. Gains in fair value are recognised only up to the amount of any losses previously recognised in the Surplus or Deficit on Provision of Services. Depreciation is not charged on Assets Held for Sale.

If assets no longer meet the criteria to be classified as Assets Held for Sale, they are reclassified back to noncurrent assets and valued at the lower of their carrying amount before they were classified as held for sale; adjusted for depreciation, amortisation or revaluations that would have been recognised had they not been classified as Held for Sale, and their recoverable amount at the date of the decision not to sell.

Assets that are to be abandoned or scrapped are not reclassified as Assets Held for Sale. When an asset is disposed of or decommissioned, the carrying amount of the asset in the Balance Sheet (whether Property, Plant and Equipment or Assets Held for Sale) is written off to the Other Operating Expenditure line in the Comprehensive Income and Expenditure Statement as part of the gain or loss on disposal. Where an Asset is fully depreciated and therefore has a zero net book value, it is deemed as being abandoned or scrapped and treated as such (This will not have an effect on the Comprehensive Income and Expenditure Statement as the gross book value and the accumulated depreciation are equal). Receipts from disposals (if any) are credited to the same line in the Comprehensive Income and Expenditure Statement also as part of the gain or loss on disposal (i.e. netted off against the carrying value of the asset at the time of disposal). Any revaluation gains accumulated for the asset in the Revaluation Reserve are transferred to the Capital Adjustment Account.

Amounts received for a disposal in excess of £10,000 are categorised as capital receipts. A proportion of receipts relating to housing disposals (75% for dwellings, 50% for land and other assets, net of statutory deductions and allowances) is payable to the Government. The balance of receipts is required to be credited to the Capital Receipts Reserve, and can then only be used for new capital investment or set aside to reduce the Authority's underlying need to borrow (the capital financing requirement). Receipts are appropriated to the Reserve from the General Fund Balance in the Movement in Reserves Statement.

The written-off value of disposals is not a charge against council tax, as the cost of fixed assets is fully provided for under separate arrangements for capital financing. Amounts are appropriated to the Capital Adjustment Account from the General Fund Balance in the Movement in Reserves Statement.

Annual Minimum Revenue Provision Statement

Where the Council finances capital expenditure by borrowing, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum provision since 2008. The Local Government Act 2003 requires the Authority to have regard to the Department for Communities and Local Government's (DCLG) Guidance on Minimum Revenue Provision issued in 2012.

The broad aim of the DCLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

For capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant assets in equal instalments, starting in the year after the asset becomes operational.

For assets acquired by finance leases or the Private Finance Initiative, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

Third party loans – Under statutory requirements the payment of the loan will normally be treated as capital expenditure. The subsequent loan repayments, (which are treated as capital receipts under statutory requirements), will be used to reduce the long term liability and consequently the CFR. As a result MRP will not generally be charged on the loan as it is not appropriate to do so.

xxi. Provisions, Contingent Liabilities and Contingent Assets

Provisions

Provisions are made where an event has taken place that gives the Authority a legal or constructive obligation that probably requires settlement by a transfer of economic benefits or service potential, and a reliable estimate can be made of the amount of the obligation. For instance, the Authority may be involved in a court case that could eventually result in the making of a settlement or the payment of compensation. Provisions are charged as an expense to the appropriate service line in the Comprehensive Income and Expenditure Statement in the year that the Authority becomes aware of the obligation, and are measured at the best estimate at the Balance Sheet date of the expenditure required to settle the obligation, taking into account relevant risks and uncertainties.

When payments are eventually made, they are charged to the provision carried in the Balance Sheet. Estimated settlements are reviewed at the end of each financial year – where it becomes less than probable that a transfer of economic benefits will now be required (or a lower settlement than anticipated is made), the provision is reversed and credited back to the relevant service.

Where some or all of the payment required to settle a provision is expected to be recovered from another party (e.g. from an insurance claim), this is only recognised as income for the relevant service if it is virtually certain that reimbursement will be received if the Authority settles the obligation.

Contingent Liabilities

A contingent liability arises where an event has taken place that gives the Authority a possible obligation whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the Authority. Contingent liabilities also arise in circumstances where a provision would otherwise be made but either it is not probable that an outflow of resources will be required or the amount of the obligation cannot be measured reliably. Contingent liabilities are not recognised in the Balance Sheet but disclosed in a note to the Accounts.

Contingent Assets

A contingent asset arises where an event has taken place that gives the Authority a possible asset whose existence will only be confirmed by the occurrence or otherwise of uncertain future events not wholly within the control of the Authority. Contingent assets are not recognised in the Balance Sheet but disclosed in a note to the Accounts where it is probable that there will be an inflow of economic benefits or service potential.

xxii. Reserves

The Authority sets aside specific amounts as reserves for future policy purposes or to cover contingencies. Reserves created by appropriating amounts out of the General Fund Balance in the Movement in Reserves Statement. When expenditure to be financed from a reserve is incurred, it is charged to the appropriate service in that year to score against the Surplus or Deficit on the Provision of Services in the Comprehensive Income and Expenditure Statement. The reserve is then appropriated back into the General Fund Balance in the Movement in Reserves Statement so that there is no net charge against council tax for the expenditure. Certain reserves are kept to manage the accounting processes for non-current assets, financial instruments, retirement, and employee benefits and do not represent usable resources for the Authority – these reserves are explained in the relevant policies.

xxiii Revenue Expenditure Funded from Capital under Statute

Expenditure incurred during the year that may be capitalised under statutory provisions but that does not result in the creation of a non-current asset has been charged as expenditure to the relevant service in the Comprehensive Income and Expenditure Statement in the year. Where the Authority has determined to meet the cost of this expenditure from existing capital resources or by borrowing, a transfer in the Movement in Reserves Statement from the General Fund Balance to the Capital Adjustment Account then reverses out the amounts charged so that there is no impact on the level of council tax.

xxiv. Schools

The *Code of Practice on Local Authority Accounting in the United Kingdom* confirms that the balance of control for local authority maintained schools (i.e. those categories of school identified in the School Standards and

Framework Act 1998, as amended) lies with the local authority. The Code also stipulates that those schools' assets, liabilities, reserves and cash flows are recognised in the local authority financial statements (and not the Group Accounts). Schools' transactions, cash flows and balances are therefore recognised in each of the financial statements of the Authority as if they were the transactions, cash flows and balances of the Authority.

xxv. VAT

VAT payable is included as an expense only to the extent that it is not recoverable from Her Majesty's Revenue and Customs. VAT receivable is excluded from income.

xxvi Fair Value Measurement

The authority measures some of its non-financial assets such as surplus assets and investment properties and some of its financial instruments such as equity shareholdings [*other financial instruments as applicable*] at fair value at each reporting date. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value measurement assumes that the transaction to sell the asset or transfer the liability takes place either:

a) in the principal market for the asset or liability, or

b) in the absence of a principal market, in the most advantageous market for the asset or liability.

The authority measures the fair value of an asset or liability using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

When measuring the fair value of a non-financial asset, the authority takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The authority uses valuation techniques that are appropriate in the circumstances and for which sufficient data is available, maximising the use of relevant observable inputs and minimising the use of unobservable inputs. Inputs to the valuation techniques in respect of assets and liabilities for which fair value is measured or disclosed in the authority's financial statements are categorised within the fair value hierarchy, as follows:

Level 1 – quoted prices (unadjusted) in active markets for identical assets or liabilities that the authority can access at the measurement date

Level 2 – inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly

Level 3 – unobservable inputs for the asset or liability.

2. Accounting Standards That Have Been Issued but Have Not Yet Been Adopted *(2019/20 Policy Document only)*

The Authority is required to disclose information relating to the impact of an accounting change that will be required by a new standard that has been issued but not yet adopted. The following key accounting policy changes has been identified:

(a) Amendments to IFRS 9 Financial instruments

Amendment relates to prepayment features with negative compensation, to make clear that amortised cost should be used where prepayments are substantially lower than the unpaid principal and interest. The Authority has no loans of this nature.

(b) Amendments to IFRS 16 – Leases

The new standard requires lessees to recognise nearly all leases on the balance sheet which will reflect their right to use an asset for a period of time and the associated liability for payments. IFRS 16 eliminates the current dual accounting model for lessees, which distinguishes between on-balance sheet finance leases and off-balance sheet operating leases. Instead, there is a single, on-balance sheet accounting model that is similar to current finance lease accounting. CIPFA/LASAAC have deferred implementation of IFRS16 for local government to 1 April 2020.

(c) Amendments to IAS 40 Investment Property - Transfers of Investment Property

This provides further explanation of the instances in which a property can be reclassified as investment property. This will have no impact on the Authority as it already complies.

(d) Other accounting standards for awareness::

IFRIC 22 Foreign Currency Transactions and Advance Consideration, IFRIC 23 Uncertainty over Income Tax Treatments, IFRS 1 First Time Adoption of International Financial Reporting Standards, IFRS 12 Disclosure of Interests in Other Entities, IAS 28 Investment in Associates and Joint Ventures. These standards do not have a material relevance for this Authority.

Havering
LONDON BOROUGH

AUDIT COMMITTEE

Subject Heading:	Head of Assurance – Progress Report 1st September – 31st December 2019
SLT Lead:	Jane West Chief Operating Officer
Report Author and contact details:	Jeremy Welburn Head of Assurance Tel: 01708 432610 / 07976539248 E-mail: jeremy.welburn@onesource.co.uk
Policy context:	To inform the Committee of progress on the assurance work during the period from 1st September – 31st December 2019.
Financial summary:	There are no financial implications arising directly from this report which is for noting and/or providing an opportunity for questions to be raised.

The subject matter of this report deals with the following Council Objectives

Communities making Havering	[X]
Places making Havering	[X]
Opportunities making Havering	[X]
Connections making Havering	[X]

SUMMARY

This report advises the Committee on the work undertaken by the Assurance Service (internal audit and counter fraud) during the period from 1st September to 31st December 2019. This report is presented in three sections:

Section 1: Introduction, Issues and Assurance opinion

Section 2: Executive Summary – A summary of the key messages

Section 3: Appendices: Provide supporting detail for Member's information

RECOMMENDATIONS

1. To note the contents of the report.

2. To raise any issues of concern and ask specific questions of officers where required.

REPORT DETAIL

Section 1: Introduction, Issues and Assurance Opinion

1.1 Introduction

1.1.1 The Accounts and Audit Regulations require the Council to undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account the Public Sector Internal Auditing Standards (PSIAS) and other guidance.

1.1.2 Internal audit is a key component of corporate governance within the Council. The three lines of defence model, as detailed below, provides a framework for understanding the role of internal audit in the overall risk management and internal control processes of an organisation:

- First line – operational management controls
- Second line – monitoring controls, e.g. the policy or system owner/sponsor
- Third line – independent assurance.

The Council's third line of defence includes internal audit, which should provide independent assurance to senior management and the Audit Committee on how effectively the first and second lines of defence have been operating.

1.1.3 An independent internal audit function will, through its risk-based approach to work, provide assurance to the Council's Audit Committee and senior management on the higher risk and more complex areas of the Council's business, allowing management to focus on providing coverage of routine operations.

1.1.4 The work of internal audit is critical to the evaluation of the Council's overall assessment of its governance, risk management and internal control systems, and forms the basis of the annual opinion provided by the Head of Assurance which contributes to the Annual Governance Statement. It can also perform a consultancy role to assist in identifying improvements to the organisation's practices.

1.1.5 This report brings together all aspects of internal audit and counter fraud work undertaken during the period from 1st September to 31st December 2019, in support of the Audit Committee's role.

1.1.6 The report supports the Head of Assurance's ongoing assurance opinion on the internal control environment and highlights key outcomes from internal audit and counter-fraud work and provides information on wider issues of interest to the Council's Audit Committee. The Appendices provide specific detail of outputs for the Committee's information.

Section 2. Executive Summary of work undertaken during the period from 1st September to 31st December 2019

2.1 Internal Audit

2.1.1 There have been ten final reports issued during this period. Of these reports, one was given no assurance, four limited assurance, four moderate and one substantial assurance. Three did not result in an opinion being provided due to the nature of the work undertaken. Appendix C shows the current position of the 2019/20 audit plan.

2.1.2 14 high risk recommendations were raised in these reports with further detail of these provided in Appendix A.

2.2 Pro-Active and Counter Fraud

2.2.1 Two of the four referrals brought forward from the previous report have been investigated. One referral has resulted in a criminal investigation and one referral had no case to answer. The remaining two are still being investigated.

2.2.2 During 1st September to 31st December 2019 two referrals were received; one referral is under investigation and for one referral there was no case to answer.

Section 3. Appendices: Provide supporting detail for Member's information

Appendix A: Detail of Internal Audit work to date
Appendix B: Detail of Counter Fraud work
Appendix C: Current status of 2019/20 audit plan

IMPLICATIONS AND RISKS

Financial implications and risks:

There are none arising directly from this report which is for noting and/or providing an opportunity for questions to be raised.

By maintaining an adequate internal audit service, management are supported in the effective identification and efficient management of risks and ultimately good governance. Failure to maximise the performance of the service may lead to losses caused by insufficient or ineffective controls or even failure to achieve objectives where risks are not mitigated. In addition recommendations may arise from any audit work undertaken and managers have the opportunity of commenting on these before they are finalised. In accepting audit recommendations, the managers are obliged to consider financial risks and costs associated with the implications of the recommendations. Managers are also required to identify implementation dates and then put in place appropriate actions to ensure these are achieved. Failure to either implement at all or meet the target date may have control implications, although these would be highlighted by any subsequent audit work. Such failures may result in financial losses for the Council.

Legal implications and risks:

There are no apparent legal implications from noting the content of this Report. However, the audit recommendations raise a number of issues which entail legal risk. The action plans set out how those risks are being mitigated.

Human Resources implications and risks:

None arising directly from this report.

Equalities implications and risks:

None arising directly from this report.

Appendix A – Progress Report - Internal Audit Work

1. Audit Progress

1.1 The Annual Audit Plan, approved by the Audit Committee in April 2019, comprised 700 audit days. The plan was developed using a thematic approach, in line with the Corporate Plan priorities for 2019/20 with time allocated under each theme to carry out risk identification and service mapping. Members are reminded that the 2019/20 audit plan was presented as a flexible plan, subject to review through the year to ensure that emerging risks are covered. Adjustments to the plan are made to allow for changes in the risk and operational environment in which the Council operates. These changes are outlined in Appendix C.

1.2 Current, cumulative progress toward delivery of the 2019/20 audit plan (excluding School Health Checks) is summarised in the table below, with further detail provided in Appendix C. It should be noted that some of the work undertaken by internal audit does not result in an opinion being provided, such as advisory reviews and grant claims.

Audit Plan Status	Number of Audits / Tasks
Final reports issued / Reviews Completed	16
Draft reports issued	2
Underway	9

2. Risk Based Systems and School Audits

The table below details the results of the final reports issued from the 1st September to 31st December 2019. A summary of the Limited Assurance / No Assurance reports and the details of the high risk recommendations raised are provided in section 3.

Report	Assurance	Recommendations			
		High	Med	Advisory	Total
System Audits					
Romford Combined Charities	N/A	0	0	0	0
Purchase Cards	Limited	1	7	0	8
Right to Buy	Moderate	0	6	0	6
School Expansion Programme	Moderate	1	2	0	3
Private Sector Leasing	No Assurance	6	3	2	11
Cloud Computing	Limited	3	10	0	13
Procurement	Limited	1	2	0	3
Financial Controls Assurance	Limited	1	0	0	1
ICT Needs Assessment	N/A	0	0	0	0
Oracle Upgrade – Phase 1	N/A	0	0	0	0
System Audits Total		**13**	**30**	**2**	**45**
School Audits					
St Ursula's RC Junior	Moderate	0	5	8	13
Newtons	Moderate	1	3	4	8
Whybridge Infants	Substantial	0	4	4	8
School Audits Total		**1**	**12**	**16**	**29**

Key to Assurance Levels	
Substantial Assurance	There is a robust framework of controls and appropriate actions are being taken to manage risks within the areas reviewed. Controls are applied consistently or with minor lapses that do not result in significant risks to the achievement of system objectives.
Moderate Assurance	Whilst there is basically a sound system of control within the areas reviewed, weaknesses were identified and therefore there is a need to enhance controls and/or their application and to improve the arrangements for managing risks.
Limited Assurance / No Assurance	There are fundamental weaknesses in the internal control environment within the areas reviewed, and further action is required to manage risks to an acceptable level.

3. Limited Assurance / No Assurance Report Summaries

3.1 Private Sector Leasing

3.1.1 **No assurance** can be given on the controls in place to manage the risks in relation to the Council's PSL scheme due to:

- Lack of legal due diligence undertaken in regard to landlords and their permissible right to lease the property;
- Lack of evidence to support completion of statutory safety checks prior to use of the property;
- Under-utilisation of properties covered by a guaranteed rent scheme and associated financial loss;
- Inconsistencies in the award of financial incentives and the continued payment of rent after the return of the property or during excessive void periods caused by the landlord;
- Absence of a process to report, record and recover repair recharges from both landlords and tenants; and
- High level of exposure to the Council of PSL related insurance claims caused by inadequate checks being carried out and / or breach of the conditions set out in the lease agreement.

3.1.2 This audit makes six high and three medium risk recommendations. Details of the high risk recommendations are outlined below.

R1	Checks undertaken prior to entering into a contractual agreement with individuals for the lease of properties should be sufficiently robust to limit risks to both tenants and the Council. **Recommendation Owner:** Darren Alexander, Head of Housing Demand **Expected Timescale for Implementation:** January 2020 **Officer's comments:** Agreed.

R2	A systematic check of existing PSLs should be carried out to ensure all key documents are in place, particularly those required to support that the property is safe for tenants to be placed in it. All documents should be stored on a suitable IT platform. Households deemed to be at risk due to living in properties that have significant faults and/or unavoidable hazards should be expected to be subject to a planned move. **Recommendation Owner:** Darren Alexander, Head of Housing Demand **Expected Timescale for Implementation:** May 2020 **Officer's comments:** Recommendation Agreed.
R3	The current strategy for identifying and recharging the historical PSL landlords repairs should be reviewed to ensure all outstanding recharges are being processed. This review should also consider whether the Council has adhered to all relevant obligations set out in the landlords lease agreement and whether the Council has a right to recharge the repair costs. **Recommendation Owner:** Darren Alexander, Head of Housing Demand **Expected Timescale for Implementation:** February 2020 **Officer's comments:** Accepted
R4	Action should be taken to implement a process for the reporting, recording and recovery of rechargeable repair costs to tenants arising from the void process. Responsibilities in relation to this process should be clearly communicated to all appropriate Teams / Officers. **Recommendation Owner:** Darren Alexander, Head of Housing Demand **Expected Timescale for Implementation:** February 2020 **Officer's comments:** Accepted
R5	A review should be undertaken of the current PSL Scheme including the Rent Guarantee Scheme and cashless bond arrangements. This should include: • The value of the cashless bond • On what terms the bond exists • When and how the bond can be redeemed • When rent payments to landlords will begin; • When rent payments will cease, including any ongoing payments of rent after the property has been handed back; • Circumstances whereby the Council would be entitled to stop rental payments e.g. in the event that the Councils ability to use the property is delayed by the owner or a suitable tenant cannot be identified; and • The payment of financial incentives and compensations payments. Expectations arising from this review should be clearly outlined in documented procedures and any associated PSL literature available to current and prospective landlords. **Recommendation Owner:** Darren Alexander, Head of Housing Demand **Expected Timescale for Implementation:** May 2020 **Officer's comments:** The policy could be completed in a shorter period however changing the literature and other publicity may take up to 6 months.

R6	The service should work with Legal Services to review the wording of the lease agreement with the property owner to ensure the Council does not assume liabilities that should rest with the landlord and to reduce the Council's risk of exposure. Advice should be sought at this time to establish how / when the Council would be in a position to replace the leases for the existing portfolio. **Recommendation Owner:** Darren Alexander, Head of Housing Demand **Expected Timescale for Implementation:** May 2020 **Officer's comments:** Resources will be needed from legal.

3.2 Cloud Computing

3.2.1 **Limited Assurance** can be given on the controls in place to manage the risks in relation to Cloud Computing due to:

- Lack of evidence to demonstrate that key stakeholders have been formally identified and are being engaged on an ongoing basis in the risk management of cloud services;
- Incomplete unsigned contract documentation, including governance responsibilities that have not been subject to review;
- Lack of information recorded within the inventory of all services provided via the cloud, such as first point of contact for addressing operational issues;
- Lack of recent testing of CSP service transition procedures as part of effective disaster recovery;
- Inconsistencies in the completion of contract monitoring meetings in line with contract arrangements including a lack of evidence to demonstrate that all key service standards are being monitored;
- Absence of established processes for detecting, reporting, responding to and learning from information security incidents;
- Out of date Document / Records Classification Policy dated November 2016, prior to the introduction of the new General Data Protection Regulation (GDPR).
- Absence of data classification prior to upload to the CSP (for Lumesse and TalentLink);
- Lack of evidence to support the formal identification of legal and regulatory requirements that must be adhered to when using CSPs.
- Lack of evidence to demonstrate that backed up data is encrypted by the CSP, or that assurance has been sought over the adequacy of physical access controls currently relied upon in the absence of physical media encryption;
- Lack of evidence to support how assurances are gained to support that data segregation occurs;
- Lack of evidence to demonstrate that formal authorisation is obtained from the employee's line manager prior to access being granted to the respective system; and
- Lack of evidence to support how new users had been assigned lifecycles to ensure lifecycles are fit for purpose and to demonstrate that auto detection and deletion of dormant user accounts, after specified days of inactivity, is currently in place.

This audit report makes two high and eleven medium risk recommendations. It should be noted that since the completion of the review, three medium and one high risk recommendations have been implemented. The high risk recommendations are outlined below:

R1	Newham and Havering Councils should obtain assurance that each CSP encrypts backed up client data. Where this is not undertaken, additional assurance should be sought from both the CSP and the shared service that back up data, at rest, is protected in accordance with the risk appetite of the two Councils. **Recommendation Owner:** Ian Gibbs **Expected Timescale for Implementation:** December 2019 **Officer's comments:** Completed
R2	User accounts should be proactively monitored to avoid having dormant or inactive accounts on all cloud applications. The Councils should systematically remove redundant users from cloud applications and maintain tighter control over operations to ensure accurate processes (housekeeping). **Recommendation Owner:** Ian Gibbs / Mark Porter **Expected Timescale for Implementation:** March 2020 **Officer's comments:** We have an automated process to look at inactive accounts that have not accessed the network. These network accounts are automatically disabled and can only be accessed via our network. The security audit in October 2018 reviewed the network security in detail and the recommendations implemented. Microsoft O365: O365 is not live for all users and we are in the process of testing and deterring its configuration. At present calls are raised using Service Manager for access to the system. Redundant accounts will be deleted and linked to the online starters and leavers process. O365 access is determined by Active Directory and we have starter, movers and leavers' process that manages access to the network and O365. Oracle: Oracle is accessed via the Council's network and is managed by Active Directory. We have a starter, mover and leaver online process. The Oracle Team is notified about changes via the online process and disables access when required. TalentLink: TalentLink is accessed via the Council's network and therefore a leaver would not be able to access the system when their network account is disabled. Data cleansing is planned for this application because a replacement system is due to be implemented in June 2020.

3.3 Procurement

3.3.1 **Limited Assurance** can be given on the controls in place to ensure compliance with legislative (OJEU Regulations) and local policies and procedures, specifically in relation to non-contracted / unapproved spend due to:

- Lack of evidence to support that a contract is in place where expected as only 11 of the 50 contracts requested could be located;
- Procurement led projects to retrospectively identify and obtain existing contracts across the Council;
- Lack of policies and procedures in place to support the agreed No Purchase Order No Pay requirement;
- Absence of Council wide communication of the No Purchase Order No Pay directive; and

- Lack of management information / exception reports being produced and disseminated to identify / monitor non-compliance;

This audit makes one high and two medium risk recommendations. The high risk recommendation is outlined below:

R1	Given the limited assurance that purchases are compliant with legislative and local policies, and the lack of evidence to support that spend is approved and achieving value for money for the Council, the Procurement function should identify how they will address all levels of non-contracted spend to ensure compliance. **Recommendation Owner:** Ross Duguid, Head of Procurement **Expected Timescale for Implementation:** **Officer's comments:**

3.4 Purchase Cards

3.4.1 **Limited Assurance** can be given on the controls in place to manage the risks in relation to the Council's Purchase Card scheme due to:

- Lack of training provided to Managers responsible for approving purchases made by cardholders;
- Lack of access to purchase card guidance via the Council's intranet;
- Absence of a clear definition of non-compliance in relation to purchase cards;
- Lack of an effective strategy for monitoring and reporting non-compliance, in accordance with the Service Level Agreement;
- Inconsistent completion of the 10% sample testing;
- Absence of links between Purchase Card Guidance and Oyster Card Guidance including the identification of work Oyster Card top ups as permitted purchase card spend;
- Gaps in procedures for the administration of purchase cards, including local actions implemented internally by the team to reduce risk, which have not been documented;
- Absence of checks undertaken on the monthly leavers list to determine whether leavers are cardholders, as a secondary control to Managers self-service responsibilities; and
- Lack of management information being reported to key stakeholders within the Council.

This audit report makes one high and seven medium risk recommendations. The high risk recommendation is outlined below.

R1	A review should be undertaken of the current service level agreement, specifically in relation to responsibilities of the team for monitoring non-compliance and the production and distribution of management information. This review should aim to: • Clarify the requirements of the usage compliance monitoring to determine whether this is limited to non-permitted spend only; and • Understand what management information the Council wants the team to produce, how often and the recipients of this information. **Recommendation Owner:** Sarah Bryant, Director of Exchequer and Transactional Services **Expected Timescale for Implementation:** **Officer's comments:**

3.5 Financial Controls Assurance

3.5.1 A high level review of the Council's financial controls was undertaken in two phases. The review considered the wider financial control environment, focusing on key financial systems and included a range of risk based audits of systems and processes, within the shared service.

3.5.2 Based on the findings of this work, **limited assurance** was placed on the Council's financial controls. As a result, a single proposed high risk action was raised, consisting of the following elements:

- The risk appetite for all key financial systems and processes should be defined as part of the project to implement Oracle Fusion;
- Consideration needs to be given to where the required key controls are owned within the first and second line of defence, and also to what timetable of assurances senior management and the s151 officer requires, based on this risk appetite;
- The resources available in the back office teams should be assessed against the requirements of the business;
- What is determined should be formally agreed so that there is clarity regarding the controls and assurances that the shared service is expected to administer. If there are differences between the requirements in Newham and in Havering, this should be clearly documented;
- Training requirements in the first and second line of defence need to be assessed and action taken;
- Future development plans, where controls enhancements are planned post go live of the new system, should be documented and monitored; and
- The agreements need to be formally reviewed, within six months after implementation, to ensure they are operating as planed and are effective.

4. Audit Recommendations Update and status of High Risk Recommendations

4.1 Internal Audit follows up all high and medium risk audit recommendations with management when the deadlines for implementation are due. There is a rolling programme of follow up work, with each auditor taking responsibility for tracking the implementation of recommendations made in their audit reports. The implementation of audit recommendations, in systems where limited assurance was provided, is verified through a follow up audit review.

4.2 This work is of high importance given that the Council's risk exposure remains unchanged if management fail to implement the recommendations raised in respect of areas of control weakness. A key element of the Audit Committee's role is to monitor the extent to which recommendations are implemented as agreed and within a reasonable timescale, with particular focus applied to any high risk recommendations.

4.3 Recommendations are classified into three potential categories according to the significance of the risk arising from the control weakness identified. The three categories comprise:

High	Fundamental control requirement needing implementation as soon as possible.
Medium	Important control that should be implemented.
Advisories	Pertaining to best practice.

4.4 All high risk recommendations (including schools) due as at 30th November 2019 have been confirmed as implemented.

Appendix B

1. Counter Fraud Audit Work – 01/09/19 to 31/12/19

1.1 Proactive Counter Fraud Investigations

1.1.1 Proactive work undertaken during 01/09/19 to 31/12/19 is shown below:

Description	Risks	Status
Advice to Directorates	General advice and support to Directors and Heads of Service including short ad-hoc investigations, audits and compliance. 13 requests for advice were received.	Ongoing
Advice to Other Local Authorities	All Data Protection Act requests via Local Authorities, Police etc. One request for advice was received.	Ongoing
Fraud Hotline	To take all telephone calls and emails relating to the 'Fraud Hotline' and refer appropriately. Two referrals were received.	Ongoing
FOI Requests	To undertake all freedom of Information Requests. No FOI requests were received.	Ongoing
National Fraud Initiative Data Upload	The 2018/19 NFI data has been downloaded and reports are being reviewed by Assurance Services or the relevant service. The NFI is an exercise that matches electronic data within and between public and private sector bodies to prevent and detect fraud and is conducted every two years.	Ongoing

1.2 Reactive Investigation Cases

1.2.1 Four referrals were brought forward from the previous period:
- One referral there was no case to answer;
- One referral has resulted in a criminal investigation; and
- Two referrals are still being investigated.

1.2.2 During 01/09/19 to 31/12/19 two referrals were received:
- One referral is under investigation;
- One referral there was no case to answer.

Audit Committee, 28 January 2020

Appendix C: Current status of 2019/20 Audit Plan

Audit Title	Status as at end Q3	Opinion	Reason for delay (where applicable)
LBH Systems Audits			
Romford Combined Charities (Additional Task)	Complete	N/A	
Payroll – Transactional Services (Key Financial Audit)	Final Report	Limited	
Financial Controls Assurance	Final Report	Limited	
Procurement (Addition to plan)	Final Report	Limited	
Purchase Card - Transactional Services	Final Report	Limited	
Right to Buy	Final Report	Moderate	
School Expansion Programme	Final Report	Moderate	
Private Sector Leasing	Final Report	No Assurance	
Corporate Governance and Decision Making	Underway		
Key Financial Audits – Compliance Work	Underway		
Treasury Management	Underway		
Corporate Health & Safety	Underway		
Pension Fund Governance	Cancelled – Based on assurances from external reviews carried out during 2019/20 (The Pensions Regulator and Hymans)		
Emergency Planning & Business Continuity	Underway		
Licensing Schemes	Underway		
Delivery of the Corporate Plan	Q4		
Safeguarding Adults	Q4		
Social Care Transitions	Q4		
Regeneration – Contract Management	Q4		
Economic Development Programme Review	Q4		
General Project Assurance	Q4		
Performance monitoring – Leisure Centres	Q4		
Post Implementation Review - Liquid Logic Children's & Adults	Q4		
Contract Management (Communities)	Q4		
Contract Management (Opportunities)	Q4		
Direct Payments – Follow Up	Underway		
Fixed Term Tenancies – Housing	Cancelled – Based on risk discussion with Director of Housing		
Shared Service Audits			
ICT needs assessment	Complete	N/A	
Oracle upgrade – Phase 1	Complete	N/A	
Oracle upgrade – Phase 2	Underway		
Cloud Computing (forms part of the ICT audit allocation)	Final Report	Limited	
Virus Protection (forms part of the ICT audit allocation)	Final Report	Moderate	

LBH Schools			
Suttons Primary	Final Report	Moderate	
Newtons Primary	Final Report	Moderate	
St Ursula's Junior	Final Report	Moderate	
Whybridge Infant	Final Report	Substantial	
Learning Federation Broadford/Mead	Draft Report		
Langtons Infant	Draft Report		
Hilldene Primary	Underway		
St. Joseph's CP	Q4		
Parklands Infant	Q4		
Crowlands Primary	Q4		
Mawney Foundation	Q4		
Harold Wood Primary	Q4		
La Salette Catholic Primary	Q4		
Health Checks (21)	4 Completed		

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