

## NOTICE OF MEETING

**Meeting:** AUDIT COMMITTEE

**Date and Time:** FRIDAY, 25 OCTOBER 2019, AT 9.30 AM\*

**Place:** COMMITTEE ROOM 1, APPLETREE COURT,  
LYNDHURST

**Telephone enquiries to:** Lyndhurst (023) 8028 5000  
023 8028 5588 - ask for Andy Rogers  
E-mail: [andy.rogers@nfdc.gov.uk](mailto:andy.rogers@nfdc.gov.uk)

### **PUBLIC PARTICIPATION:**

\*Members of the public may speak in accordance with the Council's public participation scheme:

- (a) immediately before the meeting starts, on items within the Committee's terms of reference which are not on the public agenda; and/or
  - (b) on individual items on the public agenda, when the Chairman calls that item.
- Speeches may not exceed three minutes. Anyone wishing to speak should contact the name and number shown above.

**Bob Jackson**  
Chief Executive

Appletree Court, Lyndhurst, Hampshire. SO43 7PA  
[www.newforest.gov.uk](http://www.newforest.gov.uk)

**This Agenda is also available on audio tape, in Braille, large print and digital format**

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## AGENDA

### **Apologies**

#### **1. MINUTES**

To confirm the minutes of the meeting held on 26 July 2019 as a correct record.

#### **2. DECLARATIONS OF INTEREST**

To note any declarations of interest made by members in connection with an agenda item. The nature of the interest must also be specified.

Members are asked to discuss any possible interests with Democratic Services prior to the meeting.

**3. PUBLIC PARTICIPATION**

To note any issues raised during the public participation period.

**4. INTERNAL AUDIT PROGRESS REPORT 2019/20** (Pages 1 - 18)

To receive the internal audit progress report for 2019/20.

**5. ANNUAL AUDIT LETTER FOR YEAR ENDED 31 MARCH 2019** (Pages 19 - 40)

To receive the Annual Audit Letter for year ended 31 March 2019.

**6. TREASURY MANAGEMENT MID YEAR MONITORING REPORT 2019/20**  
(Pages 41 - 52)

To note the mid year Treasury Management Monitoring report 2019/20.

**7. ICT/CYBER RISKS**

To receive a presentation on the way in which cyber threat risks are managed and monitored by the Council.

**8. DATES OF FUTURE MEETINGS**

To agree the following dates of meetings for 2020/21 (each at 9.30 a.m.)

Friday, 29 May 2020  
Friday, 24 July 2020  
Friday, 23 October 2020  
Friday, 24 January 2021  
Friday, 28 March 2021

**9. AUDIT COMMITTEE WORK PLAN** (Pages 53 - 54)

To consider the Audit Committee's Work Plan.

**10. ANY OTHER ITEMS WHICH THE CHAIRMAN DECIDES ARE URGENT**

To:

**Councillors:**

Alan O'Sullivan (Chairman)  
Emma Lane (Vice-Chairman)  
Alan Alvey  
Hilary Brand

**Councillors:**

Mahmoud Kangarani  
Martyn Levitt  
Ann Sevier  
John Ward

## AUDIT COMMITTEE – 25 OCTOBER 2019

### INTERNAL AUDIT PROGRESS REPORT 2019-20 – SEPTEMBER 2019

#### 1. INTRODUCTION

- 1.1. The purpose of this report is to provide the Audit Committee with an overview of internal audit activity completed in accordance with the approved audit plan and to provide an overview of the status of 'live' reports.

#### 2. SUMMARY

- 2.1. Under the Accounts and Audit (England) Regulations 2015, the Council is responsible for:

- ensuring that its financial management is adequate and effective and that it has a sound system of internal control which facilitates the effective exercise of functions and includes arrangements for the management of risk; and
- undertaking an adequate and effective internal audit of its accounting records and of its system of internal control in accordance with the proper practices in relation to internal control.

- 2.2. In accordance with the Public Sector Internal Audit Standards and the Council's Internal Audit Charter, the Chief Internal Auditor is required to provide a written status report to the Governance and Audit Committee, summarising:

*'communications on the internal audit activity's performance relative to its' plan.'*

- 2.3. Appendix 1 summarises the performance of Internal Audit for 2019-20 to 30 September 2019.

#### 3. FINANCIAL IMPLICATIONS

- 3.1. The audit plan consists of 470 audit days including 18 audit days provided to the New Forest National Park Authority under the current Service Level Agreement. The Council's budget for 2019-20 reflects these arrangements.

#### 4. CRIME AND DISORDER IMPLICATIONS

- 4.1. There are no crime and disorder implications arising directly from this report, however inadequate audit coverage may result in areas of control weakness, unacceptable risks or governance failings as well as the increased potential for error and fraud.

**5. ENVIRONMENTAL MATTERS & EQUALITY AND DIVERSITY IMPLICATIONS**

5.1. There are no matters arising directly from this report.

**6. RECOMMENDATION**

6.1. The Audit Committee note the content of the progress report.

**For Further Information Please Contact:**

Antony Harvey  
Deputy Head of Partnership (SIAP)  
Tel: 01962 845701  
E-mail: [antony.harvey@hants.gov.uk](mailto:antony.harvey@hants.gov.uk)

**Background Papers:**

Internal Audit Plan 19-20

**Internal Audit Progress Report**

**September 2019**

**New Forest District Council**



**Southern Internal  
Audit Partnership**

Assurance through excellence  
and innovation

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## 1. Role of Internal Audit

The requirement for an internal audit function in local government is detailed within the Accounts and Audit (England) Regulations 2015, which states that a relevant body must:

***‘Undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance.’***

The standards for ‘proper practices’ are laid down in the Public Sector Internal Audit Standards [the Standards - updated 2017].

The role of internal audit is best summarised through its definition within the Standards, as an:

***‘Independent, objective assurance and consulting activity designed to add value and improve an organisations operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes’.***

The Council is responsible for establishing and maintaining appropriate risk management processes, control systems, accounting records and governance arrangements. Internal audit plays a vital role in advising the Council that these arrangements are in place and operating effectively.

The Council’s response to internal audit activity should lead to the strengthening of the control environment and, therefore, contribute to the achievement of the organisation’s objectives.

## 2. Purpose of report

In accordance with proper internal audit practices (Public Sector Internal Audit Standards), and the Internal Audit Charter the Chief Internal Auditor is required to provide a written status report to ‘Senior Management’ and ‘the Board’, summarising:

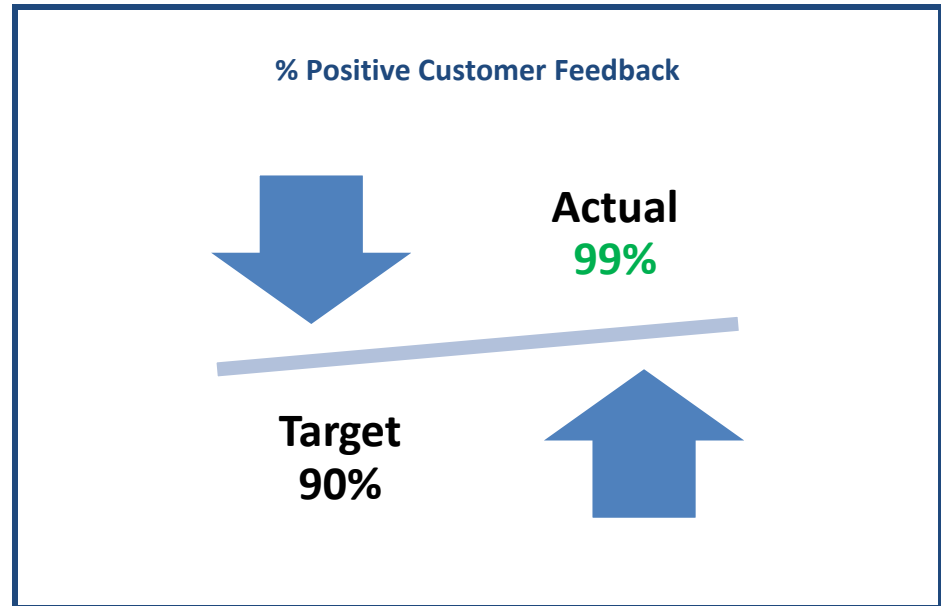
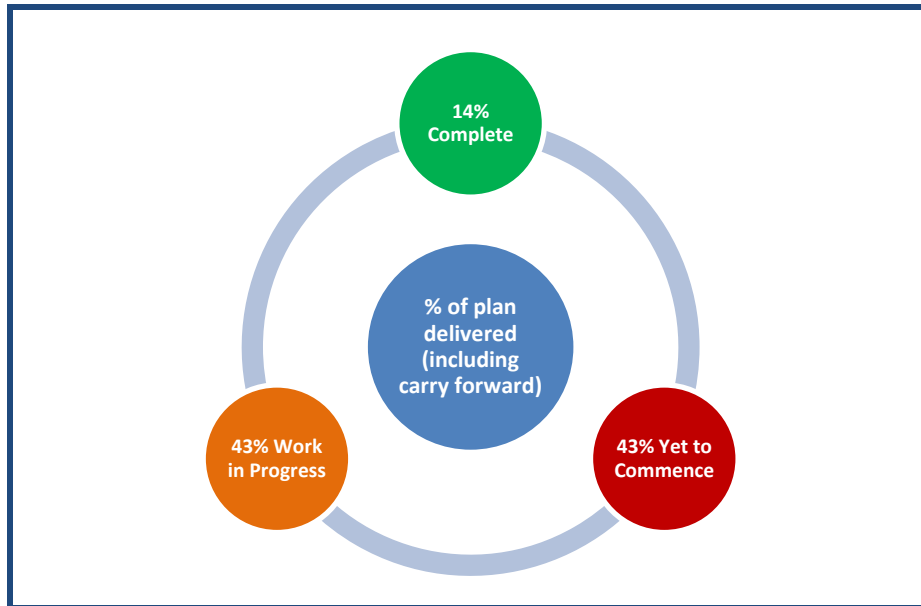
- The status of ‘live’ internal audit reports;
- an update on progress against the annual audit plan;
- a summary of internal audit performance, planning and resourcing issues; and
- a summary of significant issues that impact on the Chief Internal Auditor’s annual opinion.

Internal audit reviews culminate in an opinion on the assurance that can be placed on the effectiveness of the framework of risk management, control and governance designed to support the achievement of management objectives of the service area under review. Assurance opinions are categorised as follows:

<b>Substantial</b>	A sound framework of internal control is in place and operating effectively. No risks to the achievement of system objectives have been identified
<b>Adequate</b>	Basically a sound framework of internal control with opportunities to improve controls and / or compliance with the control framework. No significant risks to the achievement of system objectives have been identified
<b>Limited</b>	Significant weakness identified in the framework of internal control and / or compliance with the control framework which could place the achievement of system objectives at risk
<b>No</b>	Fundamental weaknesses identified in the framework of internal control or the framework is ineffective or absent with significant risk to the achievement of system objectives.



### 3. Performance dashboard



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#### Compliance with Public Sector Internal Audit Standards / Local Government Application Note



An 'External Quality Assessment' of the Southern Internal Audit Partnership was undertaken by the Institute of Internal Auditors (IIA) in September 2015. The report concluded:

*'It is our view that the Southern Internal Audit Partnership 'generally conforms' (top grading) to **all** of the principles contained within the International Professional Practice Framework (IPPF); Public Sector Internal Audit Standards (PSIAS); and the Local Government Application Note (LAGN).*

In accordance with PSIAS, a further self assessment was completed in April 2018 concluding that the Southern Internal Audit Partnership continues to comply with all aspects of the IPPF, PSIAS and LGAN.

## 4. Status of 'Live' Reports

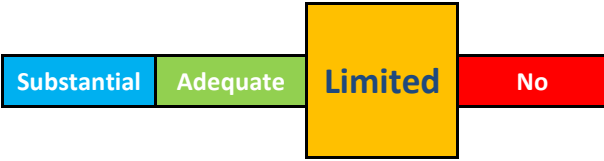
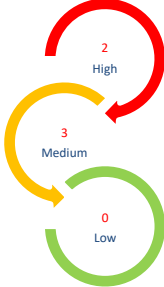
Audit Review	Report Date	Audit Sponsor	Assurance Opinion	Management Actions ('High Priority')				
				Reported	Not Accepted	Pending	Cleared	Overdue
<p>There are 18 outstanding actions relating to four audits completed by the in-house team prior to the move to SIAP (previous reported position was 28 actions from 11 audit areas). These actions will be tracked through to completion or on occasion, obsolescence if, for example, they are superseded by alternative actions to address the issues identified. Of the 18 outstanding actions, four are high priority and relate to the following areas:-</p> <ul style="list-style-type: none"> <li>• Payment Card Industry Data Security Standards (PCI DSS) Compliance. Current progress – There are elements of the current financial system and telephony system that are non-compliant. These systems are due to be replaced in 2019.</li> <li>• Business Continuity. Current progress – An initial Business Impact Analysis (BIA) has been completed with Service Managers. A proposed critical activity list has been developed and discussed with EMT. The critical activity list will be reviewed and will inform an in-depth BIA process with the aim to test Business Continuity Plans and the Emergency Response Plan during an annual exercise planned during the Spring 2019. This will be followed up by Internal Audit as part of in 2019/20 audit plan.</li> </ul>								
Environmental Services - Trade Waste	Oct -18	SM (W&T)	Limited	18 (5)	0 (0)	6 (1)	11 (4)	1 (0)
<b>Information Governance*</b>	<b>Jan-19</b>	<b>SM (L)</b>	<b>Adequate</b>	<b>2 (1)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>2 (1)</b>	<b>0 (0)</b>
<b>ICT Programme / Project Management*</b>	<b>Jan-19</b>	<b>SM (ICT)</b>	<b>Adequate</b>	<b>6 (0)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>6 (0)</b>	<b>0 (0)</b>
<b>Ethical Governance*</b>	<b>Mar-19</b>	<b>SM (DS&amp;MS)</b>	<b>Adequate</b>	<b>2 (0)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>2 (0)</b>	<b>0 (0)</b>
Risk Management	Mar-19	SM (BI&CS)	Adequate	1 (0)	0 (0)	1 (0)	0 (0)	0 (0)
Main Accounting	Mar-19	HoF	Substantial	4 (1)	0 (0)	0 (0)	3 (1)	1 (0)
<b>Housing Options – Homelessness*</b>	<b>Apr-19</b>	<b>SM (HO)</b>	<b>Adequate</b>	<b>10 (4)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>10 (4)</b>	<b>0 (0)</b>

Audit Review	Report Date	Audit Sponsor	Assurance Opinion	Management Actions ('High Priority')				
				Reported	Not Accepted	Pending	Cleared	Overdue
<b>Payroll*</b>	<b>May-19</b>	<b>SM (HR)</b>	<b>Adequate</b>	<b>1 (0)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>1 (0)</b>	<b>0 (0)</b>
Income Collection	May-19	SM (BI&CS)	Adequate	1 (0)	0 (0)	1 (0)	0 (0)	0 (0)
<b>Contract Management*</b>	<b>Jun-19</b>	<b>SM (L)</b>	<b>Adequate</b>	<b>3 (1)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>3 (1)</b>	<b>0 (0)</b>
<b>Development / Building Control*</b>	<b>Jun-19</b>	<b>SM (C&amp;PF)</b>	<b>Adequate</b>	<b>4 (1)</b>	<b>0 (0)</b>	<b>0 (0)</b>	<b>4 (1)</b>	<b>0 (0)</b>
Procurement	Jun-19	SM (L)	Adequate	4 (0)	0 (0)	1 (0)	3 (0)	0 (0)
Working in Partnership	Jun-19	SM (BI&CS)	Adequate	8 (3)	0 (0)	1 (1)	5 (2)	2 (0)
Housing Asset Management – Lift Inspection and Maintenance	Jul-19	SM (HMOps)	Limited	5 (2)	0 (0)	4 (1)	1 (1)	0 (0)

\* Denotes audits where all actions have been completed since the last progress report

Audit Sponsor		Audit Sponsor	
Service Manager (Business Improvement & Customer Services)	SM (BI&CS)	Service Manager (Housing Maintenance Operations)	SM (HMOps)
Head of Finance	HoF	Service Manager (Housing Maintenance Asset & Compliance)	SM (HMA&C)
Service Manager (Estates & Valuation)	SM (E&V)	Service Manager (Environmental & Regulation)	SM (E&R)
Service Manager (Human Resources)	SM (HR)	Service Manager (Health & Leisure)	SM (H&L)
Service Manager (Legal & Procurement)	SM(L&P)	Service Manager (Waste & Transport)	SM (W&T)
Service Manager (Democratic Services & Member Support)	SM (DS&MS)	Service Manager (Coastal & Public Facilities)	SM (C&PF)
Service Manager (Estate Management & Support)	SM (EM&S)	Service Manager (Open Spaces)	SM (OS)
Service Manager (Revenues & Benefits)	SM (R&B)	Service Manager (Planning Management Development)	SM (PMD)
Service Manager (ICT)	SM (ICT)	Service Manager (Streetscene)	SM (S)
Service Manager (Housing Options)	SM (HO)	Service Manager (Estates, Valuation & Investment Property)	SM (EV&IP)

5. Executive Summaries of new reports published concluding a ‘Limited’ or ‘No’ assurance opinion

Housing Asset Management – Lift Inspection and Maintenance		
<p><b>Audit Sponsor:</b> Ritchie Thomson – Service Manager, Housing Maintenance Operations</p> <p><b>Key Contacts:</b> Richard Fudge – Service Manager, Housing Maintenance Asset &amp; Compliance</p> <p><b>Final Report Issued:</b> 10/07/2019</p>	<p><b>Assurance opinion:</b></p> 	<p><b>Management Actions:</b></p> 
<p><b>Summary of key observations:</b></p> <p>All lifts installed prior to 2009 are the responsibility of the Council with anything after this date the responsibility of the tenant. The Facilities Management (FM) Team maintained a list of all lifts requiring inspection, which comprised of approximately 40 appliances inspected under contract with Zurich, with the FM Team retaining responsibility for managing inspections and any subsequent follow-up actions.</p> <p>Following staff changes and in preparation for the retendering of the lift inspection contract, inconsistencies were identified between data sources therefore a reconciliation of the various housing databases holding information on lifts located within Council Housing was completed by the Maintenance Strategy and Compliance Officer. This reconciliation was also compared to the FM Team routine maintenance and inspection schedule and Zurich Records which identified that approximately 100 additional domestic lifts were retained within the Council housing stock that were not part of the inspection schedule. At the time of the audit, the reconciliation and cleansing of database records had not been fully completed and the newly identified lifts had not been inspected.</p> <p>The audit also found that the lifts covered by the inspection contract with Zurich were not consistently inspected within the required review periods although once completed, lift inspection detail was received promptly from Zurich, which ensured the Council received timely notification of issues for resolution. At the time of the review, there were no formal meetings undertaken between the Council and the contractor for lift inspections therefore ongoing review of the contract was limited.</p>		

## 6. Planning & Resourcing

The Internal Audit Plan provides the mechanism through which the Chief Internal Auditor can ensure the most appropriate use of internal audit resources to provide a clear statement of assurance on risk management, internal control and governance arrangements.

The Internal Audit Plan for 2019-20 was discussed by EMT on 19 March 2019 and approved by the Audit Committee on 29 March 2019. The audit plan remains fluid to provide a responsive service that reacts to the changing needs of the Council. Progress against the plan is detailed within section 7.

## 7. Rolling Work Programme

Audit Review	Audit Sponsor	Scoping	Audit Outline Issued	Fieldwork	Draft Report Issued	Final Report Issued	Assurance Opinion	Tracker (✓ on schedule ✗ Delay)	Comment
<b>Carried forward reviews 18/19 Opinion</b>									
Programme and Project Management	SM (BI&CS)	✓	✓	✓	✓		Adequate		18/19 Opinion
Working in Partnership	SM (BI&CS)	✓	✓	✓	✓	✓	Adequate	✓	18/19 Opinion
Procurement	SM (L)	✓	✓	✓	✓	✓	Adequate	✓	18/19 Opinion
Contract Management	SM (L)	✓	✓	✓	✓	✓	Adequate	✓	18/19 Opinion
Development / Building Control	SM (C&PF)	✓	✓	✓	✓	✓	Adequate	✓	18/19 Opinion

Audit Review	Audit Sponsor	Scoping	Audit Outline Issued	Fieldwork	Draft Report Issued	Final Report Issued	Assurance Opinion	Tracker (✓ on schedule ✗ Delay)	Comment
<b>Reviews 19/20 Opinion</b>									
<b>Corporate / Cross Cutting</b>									
Financial Stability	HoF	✓						✓	
Asset Management (Appletree Property Holdings)	SM (EV&IP)							✓	Q3
Information Governance	SM (L&P)	✓						✓	
<b>Corporate governance</b>									
HR – Absence Management	SM (HR)	✓	✓	✓	✓			✓	
HR – Recruitment & Training	SM (HR)							✓	Q4
Fraud & Irregularities	HoF							✓	Q3
Health & Safety	SM (E&R)	✓						✓	
Business Continuity & Emergency Planning	SM (EM&S)							✓	Q3/Q4
<b>Core Financial Systems</b>									
Accounts Payable	HoF							✓	Q4

Audit Review	Audit Sponsor	Scoping	Audit Outline Issued	Fieldwork	Draft Report Issued	Final Report Issued	Assurance Opinion	Tracker (✓ on schedule ✗ Delay)	Comment
Accounts Receivable / Debt Management	HoF							✓	Q4
Main Accounting	HoF							✓	Q4
Payroll	SM (HR)	✓	✓	✓				✓	
Income Collection	HoF							✓	Q3
Taxation (VAT)	HoF							✓	Q4
New Finance System implementation	HoF	✓	✓	✓				✓	
<b>Information Technology</b>									
Software licensing / Management of assets	SM (ICT)							✓	Q3
Cyber security	SM (ICT)	✓						✓	
Business Continuity / Disaster Recovery Planning	SM (ICT)							✓	Q4
Service Desk and Incident Management	SM (ICT)	✓						✓	



Audit Review	Audit Sponsor	Scoping	Audit Outline Issued	Fieldwork	Draft Report Issued	Final Report Issued	Assurance Opinion	Tracker (✓ on schedule ✗ Delay)	Comment
PCI DSS consultancy	SM (ICT)	n/a	n/a	✓				✓	On-going advisory role
Web Payments Outage*	SM (ICT) & HoF	✓	n/a	✓	✓	✓	n/a	✓	Position Statement - Advice
<b>Portfolio Themes</b>									
Fleet Management	SM (W&T)	✓	✓	✓				✓	
Homelessness & Affordable Housing	SM (HO)							✓	Q3-4
Housing Asset Management – Lift Maintenance	SM (HM)	✓	✓	✓	✓	✓	Limited	✓	NB review carried forward from 18/19
Housing Asset Management	SM (HM)							✓	Q4
Housing Finance	SM (HO)							✓	Q3-4
Housing Maintenance – Supply Chain Arrangements*	SM (HM)							✓	Q3-4
Sports & Health Development	SM (H&L)							✓	Q3
Environmental Services (Trade Waste) – Follow Up Review	SM (W&T)	✓	✓	✓				✓	
Environmental and Regulation – (Food & Safety and Environmental Protection)	SM (E&R)	✓	✓	✓	✓			✓	

Audit Review	Audit Sponsor	Scoping	Audit Outline Issued	Fieldwork	Draft Report Issued	Final Report Issued	Assurance Opinion	Tracker (✓ on schedule ✗ Delay)	Comment
Licensing	SM (E&R)	✓						✓	
Planning (incl. Community Infrastructure Levy)	SM (PMD)							✓	Q4
Parking & Enforcement	SM (S)	✓	✓	✓	✓			✓	
Land Charges	SM (PMD)	✓						✓	
Grants Awarded	HoF	✓	✓	✓				✓	
Community Safety	SM (EM&S)	✓						✓	
Lease Income*	SM (EV&IP)							✓	Q3

#### Audit reviews added to the plan (included in rolling work programme above)

Lease Income*	Management request to bring forward review as lease income has not been reviewed during the last 3 years or since the move from manual to electronic system for managing leases. Audit to include lease renewals, rent reviews etc.
Housing Maintenance – Supply Chain Arrangements*	Requested by management. Audit to include end to end process for supply of goods / consumables to support housing maintenance and repairs.
Web Payments Outage*	Independent assessment/critical friend role requested by management into causes of outage and proposed future mitigations.

Proposed \*

Audit reviews removed from the plan (excluded from rolling work programme above)	
Corporate Plan*	Review in 20/21 once new Corporate Plan has been approved and performance frameworks are aligned to delivery of the new plan.
Transformation*	There is no formal transformation plan so cover under individual reviews of significant projects were required.
Establishment reviews*	No management concerns at present and lower risk reviews therefore utilise audit time on higher priority reviews.

Proposed \*

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# New Forest District Council

Annual Audit Letter for the year  
ended 31 March 2019

August 2019



Building a better  
working world

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Focused on your future



Public Sector Audit Appointments Ltd (PSAA) have issued a 'Statement of responsibilities of auditors and audited bodies'. It is available from the Chief Executive of each audited body and via the PSAA website ([www.psa.co.uk](http://www.psa.co.uk)).

This Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The 'Terms of Appointment (updated April 2018)' issued by PSAA set out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and statute, and covers matters of practice and procedure which are of a recurring nature.

This Annual Audit Letter is prepared in the context of the Statement of responsibilities and Terms of Appointment. It is addressed to the Members of the audited body, and is prepared for their sole use. We, as appointed auditor, take no responsibility to any third party.

Our Complaints Procedure - If at any time you would like to discuss with us how our service to you could be improved, or if you are dissatisfied with the service you are receiving, you may take the issue up with your usual partner or director contact. If you prefer an alternative route, please contact Steve Varley, our Managing Partner, 1 More London Place, London SE1 2AF. We undertake to look into any complaint carefully and promptly and to do all we can to explain the position to you. Should you remain dissatisfied with any aspect of our service, you may of course take matters up with our professional institute. We can provide further information on how you may contact our professional institute.



01

# Executive Summary



# Executive Summary

We are required to issue an annual audit letter to the New Forest District Council (the Council) following completion of our audit procedures for the year ended 31 March 2019. Below are the results and conclusions on the significant areas of the audit process.

Area of Work	Conclusion
<b>Opinion on the Council's:</b>	Unqualified - the financial statements give a true and fair view of the financial position of the Council as at 31 March 2019 and of its expenditure and income for the year then ended
▶ Financial statements	
▶ Consistency of other information published with the financial statements	Other information published with the financial statements was consistent with the Annual Accounts
<b>Concluding on the Council's arrangements for securing economy, efficiency and effectiveness</b>	We concluded that you have put in place proper arrangements to secure value for money in your use of resources

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Area of Work	Conclusion
<b>Reports by exception:</b>	
▶ Consistency of Governance Statement	The Governance Statement was consistent with our understanding of the Council
▶ Public interest report	We had no matters to report in the public interest
▶ Written recommendations to the Council, which should be copied to the Secretary of State	We had no matters to report
▶ Other actions taken in relation to our responsibilities under the Local Audit and Accountability Act 2014	We had no matters to report

Area of Work	Conclusion
<b>Reporting to the National Audit Office (NAO) on our review of the Council's Whole of Government Accounts return (WGA).</b>	We had no matters to report. The Council is below the specified audit threshold of £500m. Therefore, we did not perform any audit procedures on the consolidation pack.



## Executive Summary (cont'd)

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As a result of the above we have also:

Area of Work	Conclusion
Issued a report to those charged with governance of the Council communicating significant findings resulting from our audit.	Our Audit Results Report was presented on 26 July 2019.
Issued a certificate that we have completed the audit in accordance with the requirements of the Local Audit and Accountability Act 2014 and the National Audit Office's 2015 Code of Audit Practice.	Our certificate was issued on 29 July 2019.

We would like to take this opportunity to thank the Council's staff for their assistance during the course of our work.



## 02 Purpose and Responsibilities



# Purpose and Responsibilities

## The Purpose of this Letter

The purpose of this annual audit letter is to communicate to Members and external stakeholders, including members of the public, the key issues arising from our work, which we consider should be brought to the attention of the Council.

We have already reported the detailed findings from our audit work in our 2018/19 Audit Results Report to the 26 July 2019 Audit Committee, representing those charged with governance. We do not repeat those detailed findings in this letter. The matters reported here are the most significant for the Council.

## Responsibilities of the Appointed Auditor

Our 2018/19 audit work has been undertaken in accordance with the Audit Plan that we presented on 25 January 2019 and is conducted in accordance with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office.

As auditors we are responsible for:

- ▶ Expressing an opinion:
  - ▶ On the 2018/19 financial statements; and
  - ▶ On the consistency of other information published with the financial statements.
- ▶ Forming a conclusion on the arrangements the Council has to secure economy, efficiency and effectiveness in its use of resources.
- ▶ Reporting by exception:
  - ▶ If the annual governance statement is misleading or not consistent with our understanding of the Council;
  - ▶ Any significant matters that are in the public interest;
  - ▶ Any written recommendations to the Council, which should be copied to the Secretary of State; and
  - ▶ If we have discharged our duties and responsibilities as established by the Local Audit and Accountability Act 2014 and Code of Audit Practice.

Alongside our work on the financial statements, we also review and report to the National Audit Office (NAO) on you Whole of Government Accounts return. The Council is below the specified audit threshold of £500m. Therefore, we did not perform any audit procedures on the return.

## Responsibilities of the Council

The Council is responsible for preparing and publishing its statement of accounts accompanied by an Annual Governance Statement. In the AGS, the Council reports publicly each year on how far it complies with its own code of governance, including how it has monitored and evaluated the effectiveness of its governance arrangements in year, and any changes planned in the coming period.

The Council is also responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.



**03**

**Financial Statement Audit**

## Key Issues

The Council's Statement of Accounts is an important tool for the Council to show how it has used public money and how it can demonstrate its financial management and financial health. We audited the Council's Statement of Accounts in line with the National Audit Office's 2015 Code of Audit Practice, International Standards on Auditing (UK and Ireland), and other guidance issued by the National Audit Office and issued an unqualified audit report on 29 July 2019. Our detailed findings were reported to the 26 July 2019 Audit Committee.

The key issues identified as part of our audit were as follows:

Significant Risk	Conclusion
<p><b>Misstatements due to fraud or error</b></p> <p>The financial statements as a whole are not free of material misstatements whether caused by fraud or error.</p> <p>As identified in ISA (UK and Ireland) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.</p>	<p>Our approach focused on:</p> <ul style="list-style-type: none"> <li>▶ Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements</li> <li>▶ Assessing accounting estimates for evidence of management bias, and</li> <li>▶ Evaluating the business rationale for significant unusual transactions.</li> </ul> <p>Further to this, we have:</p> <ul style="list-style-type: none"> <li>▶ Inquired of management about risks of fraud and the controls put in place to address those risks, as well as gaining an understanding the oversight given by those charged with governance of management's processes over fraud.</li> <li>▶ Understood the oversight given by those charged with governance of management's processes over fraud.</li> <li>▶ Considered the effectiveness of management's controls designed to address the risk of fraud.</li> </ul> <p>We did not identify any material weaknesses in controls or evidence of material management override.</p> <p>We did not identify any instances of inappropriate judgements being applied.</p> <p>We did not identify any other transactions during our audit which appeared unusual or outside the Council's normal course of business</p>

# Financial Statement Audit (cont'd)

The key issues identified as part of our audit were as follows: (cont'd)

Significant Risk	Conclusion
<p><b>Risk of fraud in revenue recognition - inappropriate capitalisation of revenue expenditure</b></p> <p>Auditing standards also required us to presume that there is a risk that revenue and expenditure may be misstated due to improper recognition or manipulation.</p> <p>From our risk assessment, we assessed that the risk manifest itself through the potential to inappropriately capitalise revenue expenditure to improve the financial position of the general fund.</p>	<p>Our approach focused on:</p> <ul style="list-style-type: none"> <li>▶ We selected a sample of PPE additions to test and confirm the item was appropriate to capitalise through agreement to evidence such as invoices and capital expenditure authorisations.</li> <li>▶ We selected a sample of REFCUS items to test to confirm the appropriateness of the classification of these items</li> <li>▶ When performing journals testing, we analysed entries that would be classed as high risk transactions, such as items originally recorded as revenue expenditure and subsequently capitalised or reclassified as REFCUS.</li> </ul> <p>We concluded</p> <ul style="list-style-type: none"> <li>▶ PPE additions tested met the criteria under IAS16 to capitalise.</li> <li>▶ REFCUS expenditure was correctly categorised</li> <li>▶ Our testing did not identify any inappropriate transactions between revenue expenditure and capital or REFCUS codes.</li> </ul>

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Other Key Findings	Conclusion
<p>Property, Plant and Equipment and Council Dwellings valuation</p>	<p>The Authority had not valued its PPE as at the balance sheet date, so we undertook procedures to ensure it was still materially correctly stated.</p> <p>Our work performed did not identify any material misstatement, the fair value of Property, Plant and Equipment were recorded correctly in the balance sheet.</p> <p>Our work performed over the valuation of Council Dwellings did not identify any material misstatements.</p>
<p>Pension Liability</p>	<p>In order to produce their IAS19 report the pension actuary takes data from earlier in the year, and estimates the value of the pension assets and liabilities as at the year-end.</p> <p>Our testing identified that the value of the Pension Fund as at 31 March 2019 differed from the actuary's estimate, however NFDC's share of that variance was only £191,000. This was considered not material to the accounts by management and therefore they remained unadjusted.</p> <p>A £3m adjustment was made to the pension liability based on the McCloud Judgement. This item was considered to be a "post balance sheet event" which has been adjusted for, rather than a misstatement.</p> <p>NFDC made no adjustment for the expected impact of GMP on the pension liability. We estimated the impact to be £535k which management considered to be not material to the accounts and therefore has remained unadjusted. This item was not recorded in the Audit Results Report as it was calculated post committee date.</p>

# Financial Statement Audit (cont'd)

Other Key Findings	Conclusion
New Accounting Standards	<p>Our testing identified £13.735m of pooled funds held at Fair Value through Other Comprehensive Income. The Council's rationale, based on advice from its Treasury Management advisors, was that these met the definition of 'equity' and could be elected to be treated in this way. We did not agree these met the definition of equity, and therefore we considered these investments should be held at Fair Value through Profit or Loss under IFRS 9.</p> <p>Our disagreement with this treatment was a longstanding view which we had communicated previously, for example in both prior and current year accounting workshops. It is a consistent view across all auditor firms.</p> <p>Following consultations with experts by both parties, no information was provided that amended our view.</p> <p>We considered this a potential qualification matter; even though the impact on the CIES was not material this year, the classification was materially incorrect and in future years any significant market fluctuations may have lead to incorrect accounting treatment.</p> <p>The Council agreed to amend the financial statements.</p> <p>Following this adjustment, we were able to conclude that the Financial Statements had been adequately updated to reflect the new accounting standards.</p>

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## Our application of materiality

When establishing our overall audit strategy, we determined a magnitude of uncorrected misstatements that we judged would be material for the financial statements as a whole.

Item	Thresholds applied
Planning materiality	<p>We determined planning materiality to be £2.324m (2018: £2.143m), which is 2% of gross expenditure reported in the accounts.</p> <p>We consider gross expenditure to be one of the principal considerations for stakeholders in assessing the financial performance of the Council.</p>
Reporting threshold	We agreed with the Audit Committee that we would report to the Committee all audit differences in excess of £116k (2018: £107k)



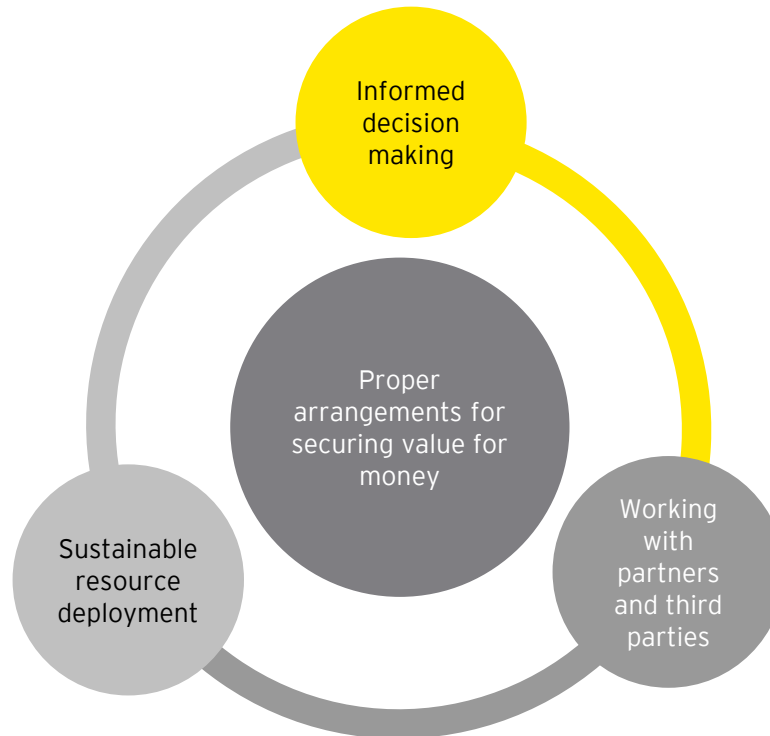
# 04 Value for Money



We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- ▶ Take informed decisions;
- ▶ Deploy resources in a sustainable manner; and
- ▶ Work with partners and other third parties.



We did not identify any significant risks in relation to these criteria. We have performed the procedures outlined in our audit plan. We did not identify any significant weaknesses in the Council's arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We therefore issued an unqualified value for money conclusion on 29 July 2019.



## 05 Other Reporting Issues



## Other Reporting Issues

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### Whole of Government Accounts

The Council is below the specified audit threshold of £500m. Therefore, we did not perform any audit procedures on the consolidation pack.

### Annual Governance Statement

We are required to consider the completeness of disclosures in the Council's annual governance statement, identify any inconsistencies with the other information of which we are aware from our work, and consider whether it is misleading.

We completed this work and did not identify any areas of concern.

### Report in the Public Interest

We have a duty under the Local Audit and Accountability Act 2014 to consider whether, in the public interest, to report on any matter that comes to our attention in the course of the audit in order for it to be considered by the Council or brought to the attention of the public.

We did not identify any issues which required us to issue a report in the public interest.

### Written Recommendations

We have a duty under the Local Audit and Accountability Act 2014 to designate any audit recommendation as one that requires the Council to consider it at a public meeting and to decide what action to take in response.

We did not identify any issues which required us to issue a written recommendation.



## Other Reporting Issues (cont'd)

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### Objections Received

We did not receive any objections to the 2018/19 financial statements from members of the public.

### Other Powers and Duties

We identified no issues during our audit that required us to use our additional powers under the Local Audit and Accountability Act 2014.

### Independence

We communicated our assessment of independence in our Audit Results Report to the Audit Committee on 26 July 2019. In our professional judgement the firm is independent and the objectivity of the audit engagement partner and audit staff has not been compromised within the meaning regulatory and professional requirements.

### Control Themes and Observations

As part of our work, we obtained an understanding of internal control sufficient to plan our audit and determine the nature, timing and extent of testing performed. Although our audit was not designed to express an opinion on the effectiveness of internal control, we are required to communicate to you significant deficiencies in internal control identified during our audit.

We have adopted a fully substantive approach and have therefore not tested the operation of controls.

Our audit did not identify any controls issues to bring to the attention of the Audit Committee.



# 07 Focused on your future



## Focused on your future

The Code of Practice on Local Authority Accounting in the United Kingdom introduces the application of new accounting standards in future years. The impact on the Council is summarised in the table below.

Standard	Issue	Impact
<b>IFRS 16 Leases</b>	<p>It is currently proposed that IFRS 16 will be applicable for local authority accounts from the 2020/21 financial year.</p> <p>Whilst the definition of a lease remains similar to the current leasing standard; IAS 17, for local authorities who lease a large number of assets the new standard will have a significant impact, with nearly all current leases being included on the balance sheet.</p> <p>There are transitional arrangements within the standard and although the 2020/21 Accounting Code of Practice for Local Authorities has yet to be issued, CIPFA have issued some limited provisional information which begins to clarify what the impact on local authority accounting will be. Whether any accounting statutory overrides will be introduced to mitigate any impact remains an outstanding issue.</p>	<p>Until the 2020/21 Accounting Code is issued and any statutory overrides are confirmed there remains some uncertainty in this area.</p> <p>However, what is clear is that the Council will need to undertake a detailed exercise to identify all of its leases and capture the relevant information for them. The Council must therefore ensure that all lease arrangements are fully documented.</p>
<b>IASB Conceptual Framework</b>	<p>The revised IASB Conceptual Framework for Financial Reporting (Conceptual Framework) will be applicable for local authority accounts from the 2019/20 financial year.</p> <p>This introduces;</p> <ul style="list-style-type: none"> <li>- new definitions of assets, liabilities, income and expenses</li> <li>- updates for the inclusion of the recognition process and criteria and new provisions on derecognition</li> <li>- enhanced guidance on accounting measurement bases</li> <li>- enhanced objectives for financial reporting and the qualitative aspects of financial information.</li> </ul> <p>The conceptual frameworks is not in itself an accounting standard and as such it cannot be used to override or disapply the requirements of any applicable accounting standards.</p> <p>However, an understanding of concepts and principles can be helpful to preparers of local authority financial statements when considering the treatment of transactions or events where standards do not provide specific guidance, or where a choice of accounting policies is available.</p>	<p>It is not anticipated that this change to the Code will have a material impact on Local Authority financial statements.</p> <p>However, Authorities will need to undertake a review to determine whether current classifications and accounting remains valid under the revised definitions.</p>



**08**

**Audit Fees**

## Audit Fees

Our fee for 2017/18 is in line with the scale fee set by the PSAA and reported in our Audit Plan.

Description	Final Fee 2018/19 £	Planned Fee 2018/19 £	Scale Fee 2018/19 £	Final Fee 2017/18 £
Total Audit Fee	44,103*	42,721	42,721	56,461

### Impact of IFRS changes\*

Our work with the Council to come to an agreement on the correct accounting for Pooled Funds involved the use of EY experts and additional hours of work in documenting and communicating our conclusions. We have specified a SFV of £1k in relation to this work.

### Additional procedures required relating to Housing Benefit expenditure\*

To obtain sufficient assurance over housing benefits expenditure and subsidy income in the Council's financial statements, we were required to undertake some elements of the work which in prior years formed part of the housing benefit subsidy claim certification process. As this work would previously have been covered by the certification fee and used additionally to provide assurance for the main audit, additional hours have been involved in completing this work. We have specified a SFV of £382 in relation to this work.

Any additional fee will be subject to approval by the PSAA.

*All fees exclude VAT*



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AUDIT COMMITTEE - 25 OCTOBER 2019

## TREASURY MANAGEMENT MID-YEAR MONITORING REPORT 2019/20

### 1. PURPOSE

- 1.1. New Forest District Council adopts the key recommendations of the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management in the Public Services: Code of Practice, last updated in 2017. The CIPFA code requires the Council to approve a treasury management strategy before the start of the year and semi-annual and annual treasury management reports.

### 2. SUMMARY

- 2.1. The Council's Treasury Management Strategy (TMS) for 2019/20 was approved at a meeting of the Council in February 2019. The Council has borrowed and invested sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

- 2.2. Treasury management in the context of this report is defined as:

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

- 2.3. Hampshire County Council's Investments & Borrowing Team has been contracted to manage the Council's treasury management balances since March 2014 but overall responsibility for treasury management remains with the Council. No treasury management activity is without risk and the effective identification and management of risk are integral to the Council's treasury management objectives.

- 2.4. All treasury activity has complied with the Council's revised Treasury Management Strategy and Investment Strategy for 2018/19, and all relevant statute, guidance and accounting standards. In addition, support in undertaking treasury management activities has been provided by the Council's treasury advisers, Arlingclose.

### 3. EXTERNAL CONTEXT

- 3.1. The following sections outline the key economic themes currently in the UK against which investment and borrowing decisions have been made to date in 2019/20.

## **Economic commentary**

- 3.2. UK Consumer Price Inflation (CPIH) fell to 1.7% year on year in August 2019 from 2.0% in July, weaker than the consensus forecast of 1.9% and below the Bank of England's target.
- 3.3. Labour market data for the three months to July 2019 showed the unemployment rate edged back down to 3.8% while the employment rate remained at 76.1%, the joint highest since records began in 1971. Once adjusted for inflation, real wages were up 1.9% on an annual basis as wages continue to rise steadily and provide some upward pressure on general inflation.
- 3.4. There was a contraction of 0.2% in quarterly GDP growth in the second calendar quarter of 2019 following the 0.5% gain in Q1, which was distorted by stockpiling ahead of Brexit. Only the services sector registered an increase in growth, a very modest 0.1%, with both production and construction falling and the former registering its largest drop since Q4 2012. Business investment fell by 0.4% (revised from -0.5% in the first estimate) as Brexit uncertainties impacted on business planning and decision-making.
- 3.5. The Bank of England maintained Bank Rate at 0.75% and in its August Inflation Report noted the deterioration in global activity and sentiment and confirmed that monetary policy decisions related to Brexit could be in either direction depending on whether or not a deal is ultimately reached by 31st October.
- 3.6. Globally, the European Central Bank cut its deposit rate by 10 basis points in September 2019 alongside announcing another round of stimulus, which was closely followed by a 25 basis points cut by the US Federal Reserve.

## **Financial Markets**

- 3.7. After rallying early in 2019, financial markets have been adopting a more risk-off approach in the following period as equities saw greater volatility and bonds rallied (prices up, yields down) in a flight to quality and anticipation of more monetary stimulus from central banks.
- 3.8. Gilt yields remained volatile over the period on the back of ongoing economic and political uncertainty. From a yield of 0.63% at the end of June, the 5-year benchmark gilt yield fell to 0.32% by the end of September. There were falls in the 10-year and 20-year gilts over the same period, with the former dropping from 0.83% to 0.55% and the latter falling from 1.35% to 0.88%. 1-month, 3-month and 12-month LIBID (London Interbank Bid) rates averaged 0.65%, 0.75% and 1.00% respectively over the period.
- 3.9. Recent activity in the bond markets and PWLB interest rates highlight that weaker economic growth remains a global risk. The US yield curve remains inverted with 10-year Treasury yields lower than US 3-month bills. History has shown that a recession hasn't been far behind a yield curve inversion. Following the sale of 10-year Bunds at -0.24% in June, yields on German government securities continue to remain negative in

the secondary market with 2 and 5-year securities currently both trading around -0.77%.

### Credit background

3.10. Credit Default Swap (CDS) spreads rose and then fell again during the quarter, continuing to remain low in historical terms. After rising to almost 120bps in May, the spread on non-ringfenced bank NatWest Markets plc fell back to around 80bps by the end of September, while for the ringfenced entity, National Westminster Bank plc, the spread remained around 40bps. The other main UK banks, as yet not separated into ringfenced and non-ringfenced from a CDS perspective, traded between 34 and 76bps at the end of the period.

3.11. There were minimal credit rating changes during the period. Moody's upgraded The Co-operative Bank's long-term rating to B3 and Fitch upgraded Clydesdale Bank and Virgin Money to A-.

## 4. LOCAL CONTEXT

4.1. On 31 March 2019, the Council had net borrowing of £77.0m. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. These factors are summarised in Table 1 below:

Table 1: Balance Sheet Summary

	31/03/2019 Balance £m
General Fund CFR	(4.9)
Housing Revenue Account CFR	(1.9)
HRA Settlement	(134.5)
Total CFR	(141.3)
Less: Resources for investment	64.3
Net borrowing	(77.0)

4.2. The Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing, in order to reduce risk and keep interest costs low. The treasury management position as at 31 August 2019 and the year-on-year change is shown in Table 2 below:

Table 2: Treasury Management Summary

	31/03/2019 Balance £m	Movement £m	31/08/2019 Balance £m	31/08/2019 Rate %
Long-term borrowing	(131.2)	-	(131.2)	(3.25)
Short-term borrowing	(4.3)	-	(4.3)	(1.99)
Total borrowing	(135.5)	-	(135.5)	(3.21)
Long-term investments	28.6	(4.0)	24.6	3.16
Short-term investments	28.7	11.3	40.0	1.04
Cash and cash equivalents	6.8	2.9	9.7	0.73
Total investments	64.1	10.2	74.3	1.70
Net borrowing	(71.4)	10.0	(61.2)	

Note: the figures in the table above are from the balance sheet in the Council's statement of accounts, but adjusted to exclude operational cash, accrued interest and other accounting adjustments.

- 4.3. The reduction in net borrowing of £10.2m shown in Table 2 above reflects an increase in investment balances of £10.2m. The increase in total investments since 31 March 2019 reflects the fluctuating cash position that is seen by the Council through the course of a financial year and the fact that the balance at 31 March is typically the lowest of the year.

## 5. BORROWING ACTIVITY

- 5.1. As shown in Table 2, at 31 August 2019 the Council held £135.5m of loans with the vast majority of loans being in relation to the resettlement of the HRA in 2012/13. The mid-year treasury management borrowing position and movement since 31 March 2019 is shown in Table 3 below.

Table 3: Borrowing Position

	31/03/2019 Balance £m	Movement £m	31/08/2019 Balance £m	31/08/2019 Rate %	31/08/2019 WAM* years
Public Works Loan Board	135.5	-	135.5	3.21	16.40
Total borrowing	135.5	-	135.5	3.21	16.40

\* Weighted average maturity

Note: the figures in the table above are from the balance sheet in the Council's statement of accounts but adjusted to exclude accrued interest.

- 5.2. The Council's chief objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.
- 5.3. In keeping with these objectives, no new borrowing was undertaken in the period to 31/08/2019. This strategy enables the Council to minimise net borrowing costs (despite foregone investment income) and reduce overall treasury risk.
- 5.4. The benefits of internal borrowing were monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Arlingclose assists the Council with the monitoring of internal and external borrowing.

## 6. INVESTMENT ACTIVITY

- 6.1. The Council holds invested funds representing income received in advance of expenditure plus balances and reserves. The Council's investment holding was £74.3m principal at 31 August 2019, which was £0.37m (0.5%) lower than the same time last year.

6.2. During the five month period from 1 April to 31 August 2019, the Council's investment balance ranged between £64m and £89m due to timing differences between income and expenditure.

6.3. Table 4 below shows investment activity for the Council as at 31 August 2019 in comparison to the reported activity as at 31 March 2019. The increase in total investments since 31 March 2019 reflects the fact that the balance at 31 March is typically the lowest of the year.

Table 4: Investment Position (Treasury Investments)

Investments	31/03/2019 Balance £m	Movement £m	31/08/2019 Balance £m	31/08/2019 Rate %	31/08/2019 WAM* years
<b>Short term Investments</b>					
Banks and Building Societies:					
- Unsecured	8.0	5.0	13.0	0.96	0.24
- Secured	5.7	4.3	10.0	1.04	0.59
- UK Treasury Bills	0.0	2.0	2.0	0.70	0.20
Money Market Funds	6.8	1.9	8.7	0.73	0.00
Local Authorities	11.0	1.0	12.0	0.93	0.34
Registered Providers	2.0	-	2.0	1.92	0.58
Cash Plus Funds	2.0	-	2.0	1.64	n/a
	<b>35.5</b>	<b>14.2</b>	<b>49.7</b>	<b>0.99</b>	<b>0.30</b>
<b>Long term investments</b>					
Banks and Building Societies:					
- Secured	7.0	(4.0)	3.0	1.00	3.45
Local Authorities	4.0	-	4.0	1.38	1.65
Registered Providers	4.0	-	4.0	1.93	<b>1.58</b>
	<b>15.0</b>	<b>(4.0)</b>	<b>7.0</b>	<b>1.47</b>	<b>2.12</b>
<b>High yield investments</b>					
Pooled Property Funds**	7.6	-	7.6	3.96	n/a
Pooled Equity Funds**	3.0	-	3.0	6.32	n/a
Pooled Multi-Asset Funds**	3.0	-	3.0	4.18	n/a
	<b>13.6</b>	<b>-</b>	<b>13.6</b>	<b>4.53</b>	<b>n/a</b>
<b>TOTAL INVESTMENTS</b>	<b>64.1</b>	<b>10.2</b>	<b>74.3</b>	<b>1.70</b>	<b>0.65</b>

\* Weighted average maturity

\*\* The rates provided for pooled fund investments are reflective of annualised income returns over the year to 30 June 2019.

Note: the figures in the table above are from the balance sheet in the Council's statement of accounts but adjusted to exclude operational cash and accrued interest.

6.4. The CIPFA Code and government guidance both require the Council to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the highest rate of return, or yield.

6.5. The Council's objective when investing is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

- 6.6. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2019/20.
- 6.7. Counterparty credit quality has been assessed and monitored with reference to credit ratings, analysis of funding structure and susceptibility to bail-in of financial institutions, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.
- 6.8. The Council also makes use of secured investment products that provide collateral in the event that the counterparty cannot meet its obligations for repayment.
- 6.9. To ensure sufficient liquidity, the Council makes use of call accounts and money market funds. With the uncertainty around Brexit, the Council will ensure there are enough accounts open at UK domiciled banks and Money Market Funds to hold sufficient liquidity and that its account with the Debt Management Account Deposit Facility (DMADF) remains available for use in an emergency.
- 6.10. The progression of credit risk and return metrics for the Council's investments managed in-house (excluding external pooled funds) are shown in the extracts from Arlingclose's quarterly investment benchmarking in Table 5 below. The comparisons with other authorities are as at 30 June 2019.

Table 5: Investment Benchmarking (investments managed in-house)

	Credit Rating	Bail-In Exposure	WAM* (days)	Rate of Return
31/03/2019	AA-	31%	325	1.11%
30/06/2019	AA-	39%	272	1.09%
Similar LAs	AA-	63%	81	0.88%
All LAs	AA-	62%	28	0.85%

\* Weighted average maturity

- 6.11. During the first five months of 2019/20, total investment balances increased by £10.2m as a result of the timing of front-loaded government grants and council tax receipts.
- 6.12. As the majority of this increase in the balance will be required over the course of the rest of the financial year, it has largely been invested in short term options, reducing the weighted average maturity of investments and increasing bail-in exposure when compared with the 31 March 2019 position.
- 6.13. The Council does, however, compare favourably with other similar local authorities as well as all local authority clients of Arlingclose on both measures. Approximately 61% of the Council's surplus cash is invested so that it is not subject to bail-in risk, with the remaining balance largely held in overnight money market funds, which are subject to reduced bail in risk. By comparison, only 37% of the cash held by other similar Local Authorities is not subject to bail-in risk.
- 6.14. The Council has targeted a proportion of funds towards high yielding investments as shown in Table 4. Investments yielding higher returns will



contribute additional income to the Council, although some come with the risk that they may suffer falls in the value of the principal invested.

- 6.15. The £13.55m portfolio of externally managed pooled multi-asset, equity and property funds generated an annualised total return of 3.52% between the start of the financial year and the end of August 2019. This total return comprised an annualised income return of 4.83% to contribute towards the revenue budget, offset by a 1.31% fall in capital values.
- 6.16. It is the Council's intention to hold these investments in pooled funds for at least the medium term and they are made in the knowledge that capital values will move both up and down in the short term, but with the confidence that over a three to five-year period total returns should exceed cash interest rates, whilst also providing regular income, diversification and the potential for capital growth.
- 6.17. Recent changes to accounting regulations (IFRS9) have introduced a new risk related to the Council's investments in pooled funds whereby any fall in the capital value of the funds would now have to be taken as an expenditure charge to the Council's Income and Expenditure account. This does not though present an immediate risk, as there is currently a statutory override in place that provides a 4 year grace period before this requirement is implemented.
- 6.18. If no further changes are made at the end of the 4 year period, the risk of a fall in value resulting in an expenditure charge for the Council will be mitigated by reserves accrued through any increases in the value of the Council's investments over the next 4 years.
- 6.19. The performance and ongoing suitability of these pooled funds in meeting the Council's investment objectives is monitored regularly and discussed with Arlingclose.

## **7. NON-TREASURY INVESTMENTS**

- 7.1. The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.
- 7.2. This could include service investments for operational and/or regeneration reasons as well as commercial investments which are made mainly for financial reasons.
- 7.3. The Council's existing non-treasury investments are listed in Table 6 below.

Table 6 – Non-Treasury Investments	31/08/19 Asset value £m	Annualised Rate of Return for 2019/20
Hythe Marina	2.54	6.26%
Saxon Inn Calmore	0.18	7.10%
Meeting House Lane	0.13	-
New Milton Health Centre	2.33	5.62%
Ampress Park Car Park	2.10	4.40%
Land at Beaumont Park	2.01	0%
<b>Total</b>	<b>9.29</b>	<b>4.00%</b>

7.4. The Council's investment property holdings total £9.29m as at 31/08/19. Two investments have been made to date in 2019; Ampress Car Park and Land at Beaumont Park. These are included within Table 6 above. Both purchases have been made pursuant to the Council's Commercial Property Strategy. The returns as shown in table 6 are inclusive of operating costs but exclude MRP (applicable to purchases made under the 2017 strategy).

## 8. COMPLIANCE REPORT

8.1. The Council confirms compliance of all treasury management activities undertaken during the period with the CIPFA Code of Practice and the Council's approved revised Treasury Management Strategy. Compliance with the authorised limit and operational boundary for external debt is demonstrated in Tables 6 below.

Table 6: Debt Limits

	2019/20 Maximum £m	31/08/2019 Actual £m	2019/20 Operational Boundary £m	2019/20 Authorised Limit £m	Complied
Total debt	135.5	135.5	186.3	201.6	✓

## 9. TREASURY MANAGEMENT INDICATORS

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

### Interest Rate Exposures

9.2. The following indicator shows the sensitivity of the Council's current investments and borrowing to a change in interest rates:

Table 7: Investment Limits

	31/08/19	Impact of +/-1% interest rate change
Variable interest rate investment exposure	£56m	+/- £0.6m
Variable interest rate borrowing exposure	£0m	n/a

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

### **Maturity Structure of Borrowing**

9.4. This indicator is set to control the Council's exposure to refinancing risk.

Table 9: Maturity Structure of Borrowing

	31/08/2019 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	3%	25%	0%	✓
12 months and within 24 months	3%	25%	0%	✓
24 months and within 5 years	10%	25%	0%	✓
5 years and within 10 years	15%	25%	0%	✓
10 years and above	69%	100%	0%	✓

### **Principal Sums Invested for Periods Longer than 365 days**

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

Table 10: Principal Sums Invested for Periods Longer than 365 days

	2019/20	2020/21	2021/22
Actual principal invested beyond year end	£25m	£21m	£18m
Limit on principal invested beyond year end	£40m	£40m	£40m
Complied	✓	✓	✓

9.6. The table includes investments in strategic pooled funds of £13.55m as although these can usually be redeemed at short notice, the Council intends to hold these investments for at least the medium-term.

## **10. OUTLOOK FOR THE REMAINDER OF 2019/20**

10.1. The global economy is entering a period of slower growth in response to political issues, primarily the trade policy stance of the US, and there appears no near-term resolution to the trade dispute between China and the US.

10.2. The UK economy has displayed a marked slowdown in growth due to both Brexit uncertainty and the downturn in global activity.

- 10.3. In response, global and UK interest rate rise expectations have eased, and central bank actions and geopolitical risks will continue to produce significant volatility in financial markets, including bond markets.
- 10.4. The Council's treasury advisor Arlingclose expects Bank Rate to remain at 0.75% for the foreseeable future but there remain substantial risks to this forecast, dependant on Brexit outcomes and the evolution of the global economy.
- 10.5. Arlingclose also expects gilt yields to remain at low levels for the foreseeable future and judge the risks to be weighted to the downside and that volatility will continue to offer longer-term borrowing opportunities.

	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22
<b>Official Bank Rate</b>													
Upside risk	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25
Arlingclose Central Cas	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75
Downside risk	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75

## 11. CRIME AND DISORDER AND ENVIRONMENTAL IMPLICATIONS

- 11.1. None arising directly from this report.

## 12. RECOMMENDATIONS

Members are recommended to:

- 12.1. consider the performance of the treasury function detailed in this report.

Further information	Background papers
Please contact Rob Sarfas (HCC), or Alan Bethune	The Prudential Code, CIPFA Guidance Notes and ODPM Investment Guidance
	Local Government Act 2003
email: rob.sarfas@hants.gov.uk <a href="mailto:alan.bethune@nfdc.gov.uk">alan.bethune@nfdc.gov.uk</a>	SI 2003/3146 Local Authorities (Capital Finance and Accounting) (England) Regulations 2003
	<p>Treasury Management Strategy Report 2019/20 Audit Committee – 25 January 2019 Council – 25 February 2019</p> <p>Treasury Management Mid-Year Monitoring Report 2018/19 Audit Committee – 6 October 2018</p> <p>Treasury Management Annual Outturn Report 2018/19 Audit Committee – 31 May 2019 Cabinet – 3 July 2019 Council – 8 July 2019</p>
	Published Papers

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## Audit Committee Work Plan 2019/20

<b>DATE</b>	<b>WORK / REPORTS</b>
24 January 2020	Internal Audit Progress Report 2019/20 Audit Plan 2019/20 Treasury Management Strategy Risk Management Regulation of Investigatory Powers Act 2000 Policy
27 March 2020	Internal Audit Progress Report 2019/20 Internal Audit Charter 2020/21 Internal Audit Plan 2020/21 AGS Action Plan - Update Bad Debt/Write-offs

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