Gateshead Council

Public Document Pack

AUDIT AND STANDARDS COMMITTEE AGENDA

Monday, 9 March 2020 at 10.00 am in the Blaydon Room - Civic Centre

From the Chief Executive, Sheena Ramsey

Item	Business
1	**Apologies for Absence**
2	**Minutes** (Pages 3 - 8) The Committee is asked to approve, as a correct record, the minutes of the meeting held on 27 January 2020.
3	**Declarations of Interest** Members of the Committee are invited to declare interests in any agenda items.
4	**Audit and Standards Committee Work Programme 2019-20** (Pages 9 - 10) The Committee is invited to review and note the current work programme.
5	**External Auditor: Audit Strategy Memorandum Year Ending 31 March 2020** (Pages 11 - 32) Report of the Strategic Director, Resources and Digital
6	**Annual Governance Statement 2019/20 - Assurance Framework** (Pages 33 - 38) Report of the Strategic Director, Resources and Digital
7	**Treasury Policy Statement and Treasury Strategy 2020/21 to 2024/25** (Pages 39 - 72) Report of the Strategic Director, Resources and Digital
8	**Date and time of next meeting** Monday 27 April 2020 at 10.00 am in the Blaydon Room, Civic Centre

Contact: Helen Conway- Tel: 0191 433 3993 - Email: helenconway@gateshead.gov.uk,
Date: Friday, 28 February 2020

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GATESHEAD METROPOLITAN BOROUGH COUNCIL

AUDIT AND STANDARDS COMMITTEE MEETING

Monday, 27 January 2020

PRESENT: Councillor M Charlton (Chair)

Councillor(s): L Green, J McClurey, J McElroy, Mr Stuart Bell (Independent Member), B Jones, D Burnett and S Green

APOLOGIES: Councillor(s): G Clark

ASC249 MINUTES SLIENCE FOR THE LATE COUNCILLOR NEIL WEATHERLEY

The Committee stood for a minute's silence in remembrance for Councillor Neil Weatherley, who was a member of this Committee and ward member for the Birtley ward, who sadly passed away on 12 December 2019 after a short illness.

ASC250 MINUTES

The minutes of the last meeting held on 28 October 2019 were approved as a correct record.

ASC251 DECLARATIONS OF INTEREST

There were no declarations of interest.

ASC252 QUARTERLY STANDARDS UPDATE

The Committee received the quarterly update highlighting national and local standards issues, and to advise members of national reviews and consultations which may be relevant to their role.

The Committee were advised that the LGA is working closely with a number of other organisations to co-ordinate a programme of work entitled 'Civility in Public Life', aimed at:

- Articulating good standards for anyone engaging in public and political discourse
- Understand the scale and impact of intimidation and abusive behaviour on our membership organisations, and develop recommendations for achieving positive debate and public-decision making on a local level

- To support our members and all democratically elected local representatives in addressing intimidation and abuse, so they can deliver the best on behalf of their communities

The LGA together with the Welsh LGA has published a guide detailing practical steps councillors and councils can take to protect themselves as a person in a public position.

The guide provides general advice on handling intimidation as well as specific situation, for example intimidation over the telephone and at ward surgeries.

The guide can be found at:
https://www.local.gov.uk/sites/default/files/documents/Full%20word%20english%20version%20guide%20for%20councillors%20on%20handling%20intimidation FINAL.pdf

RESOLVED -
i) That the information be noted
ii) That a standards update will be provided on a quarterly basis to the Audit and Standards Committee
iii) That the content of the update will vary depending on the local and national picture at that time

ASC253 LOCAL CODE OF GOVERNANCE

The Committee were requested to consider and approve an update version of the Local Code of Governance, based on the CIPFA Delivering Good Governance in Local Government Framework.

As part of this year's annual review of the Local Code of Governance, the Council's senior management have been requested to make any necessary amendments or additions to the document. As a result some amendments have been made to the Local Code of Governance as follows:

- The refresh of the Workforce Strategy and Plan have been included in the actions for Principle A (sub-principle on demonstrating strong commitments to ethical values).
- The dates on the Medium Term Financial Strategy (MTFS) have been updated to reflect the current document (Principles C, D & G)
- Reference to Vision 2030 has been deleted in Principle C.
- The Leadership and Management Development Programme have been included in the column 'We demonstrate this by' in Principle E
- Delivery of the Leadership Development Programme and Management Development Programme during 2020 have been added to the actions in Principle E

The revised Local Code of Governance was appended to the main report for information.

RESOLVED - i) That the information be noted
ii) That the updated Local Code of Governance is approved

ASC254 WORK PROGRAMME

RESOLVED – that the Committee's work programme for 2019/20 be noted

ASC255 EXTERNAL AUDITOR: AUDIT PROGRESS REPORT

The Committee received a report providing an update on Mazars progress in delivering their responsibilities as external auditor.

The report outlined:

- 2019/20 audit
- National publications

The external auditor's report was appended to the main report at Appendix A.

RESOLVED – that the contents of the external auditor's report be noted

ASC256 CORPORATE RISK MANAGEMENT 2019/20: QUARTERLY REPORT TO 31 DECEMBER 2019

The Committee received a report providing an update on developments in Corporate Risk Management during the period 1 October to 31 December 2019 in compliance with the requirements of good corporate governance.

The report covered the quarterly updates on risk management, business continuity and the work of the Council's Risk and Resilience Group.

The Committee were also advised that in order to enable comparison with other public sector organisations, the Council participated in the 2019 ALARM/CIPFA Risk Management Benchmarking Club.

Membership of the club provides access to a performance measurement tool designed to test the organisation's performance against the major risk management standards, expectations of inspection bodies and criteria that inform the risk management element of the Annual Governance Statement.

The benchmarking question set is based on ALARM's National Performance Model for Risk Management in Public Services published in 2009. The model breaks down risk management activity into seven strands and aims to provide an in-depth picture of the maturity of risk management within the organisation.

Scores of levels 1 to 5 are awarded for each strand to identify the level of maturity that the organisation has reached with level 5 being the highest possible score. The categories are as follows:

1. Awareness
2. Happening
3. Working
4. Embedded and Integrated
5. Driving

The Committee were advised that the Council has maintained the same scores as in the previous exercise undertaken in 2018, and a local action plan has been developed to address any areas for improvement identified from the process to further strengthen risk management arrangements.

RESOLVED - i) That the information be noted
ii) The Committee endorsed the effectiveness of the Council's risk management arrangements

ASC257 EXCLUSION OF THE PRESS AND PUBLIC

RESOLVED - That the press and public be excluded from the meeting during consideration of the remaining business in accordance with Paragraph 3 of Schedule 12A to the Local Government Act 1972.

ASC258 INTERNAL AUDIT PLAN 2019/20 QUARTERLY MONITORING REPORT TO 31 DECEMBER 2019

The Committee received a report outlining progress made by the Internal Audit and Risk Service against the audit plan for the financial year 2019/20 and summarising the main findings arising from audit activity throughout the period 1 October 2019 to 31 December 2019.

The report demonstrated the completion of 72% of the audit plan for Gateshead Groups and Services in terms of actual hours against planned hours to date which is on target to achieve the local performance target for completing 97.25% of actual hours against planned hours for the year.

A total of 16 assignments were completed during the period. Of the work completed, the conclusion in four cases was operating well and 12 were satisfactory.

From the reviews carried out to 31 December 2019 audit work was found to be complying with the Public Sector Internal Audit Standards and the Audit Manual.

Indicators in relation to key performance information are all either on or exceeding targets, with the exception of productive or chargeable time, which was recorded at 70% against a target of 73%, which is due to the relatively high number of bank holidays and annual leave during the first three quarters of the year.

RESOLVED - that the information be noted

ASC259 DATE AND TIME OF NEXT MEETING

The next meeting will be held on Monday 9 March 2020 at 10.00 am in the Blaydon Room.

Chair……..

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AUDIT AND STANDARDS COMMITTEE

WORK PROGRAMME

Committee Meeting Date and Time	**Items to be considered**
9 March 2020 10.00am	• Work Programme • Treasury Policy Statement and Treasury Strategy • Annual Governance Statement 2019/20 - Assurance Framework • External Auditor: Audit Strategy Memorandum Year Ending 31 March 2020
27 April 2020 10.00am	• Work Programme • Standards Update • Mazars Audit Progress Report • Internal Audit Charter, Strategy Statement and Annual Plan 2020/21 • Corporate Risk Management 2019/20 Quarterly Report to 31 March 2020 • Internal Audit Plan 2019/20 Quarterly Monitoring Report to 31 March 2020 (exempt item)
22 June 2020 10.00am	• Constitution • Role and Remit • Work Programme • Treasury Annual Report 2019/20 • Mazars Audit Progress Report • Oversight of Management Processes • Members' Assurance Statements 2019/20 • Managers' Assurance Statements 2019/20 • Review of the Effectiveness of Internal Audit 2019/20 • Corporate Risk Management – Annual Report 2019/20 • Internal Audit Annual Report 2019/20 (exempt item) • Annual Governance Statement 2019/20
20 July 2020 10.00am	• Work Programme • Standards Update • Audit Completion Report Year Ended 31 March 2020 and Gateshead Council Statement of Accounts 2019/20 • Annual Report to Cabinet and Council 2019/20 • Corporate Risk Management 2020/21 – Quarterly Report to 30 June 2020 • Internal Governance Statement 2019/20 – Internal Audit Review of Managers' Assurances • Internal Audit Plan 20120/21 – Quarterly Monitoring Report to 30 June 2020 (Exempt Item)

19 October 2020 10.00am	• Work Programme • Standards Update • Results of the 2019/20 CIPFA Audit Benchmarking • External Auditor Annual Audit Letter 2019/20 • Corporate Risk Management 2020/21 - Quarterly Report to 30 September 2020 • Treasury Management – Performance to 30 September 2020 • Internal Audit Plan 2020/21 – Quarterly Monitoring Report to 30 September 2020 (Exempt Item) • Mid Year Fraud Update 2020/21 (Exempt Item)
25 January 2021 10.00am	• Work Programme • Standards Update • Local Code of Governance • Mazars Audit Progress Report • Mazars – Results of Certification Work 2019/20 • Corporate Risk Management 202021 – Quarterly Report to 31 December 2020 Internal Audit Plan 2019/20 – Quarterly Monitoring Report to 31 December 2020 (Exempt Item)

Audit and Standards Committee
9 March 2020

Title of Report: **External Auditor: Audit Strategy Memorandum Year Ending 31 March 2020**

Report of: **Darren Collins, Strategic Director, Resources and Digital**

Purpose of the Report

1 This report requests that the Committee note the external auditor's Audit Strategy Memorandum for the year ended 31 March 2020.

Background

2 The report sets out:

- A summary of the engagement and responsibilities
- The audit engagement team
- Audit scope, approach and timelines;
- Significant risks and key judgements areas;
- Value for Money;
- Fees for audit and other services;
- Commitment to independence; and
- Materiality and misstatements.

3 The external auditor's report is attached at Appendix A.

Recommendation

4 The Committee is requested to note the contents of the external auditor's Audit Strategy Memorandum.

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Audit Strategy Memorandum

Gateshead Council and Group

Year ending 31 March 2020

Gateshead Council

MAZARS

CONTENTS

Mazars LLP
Salvus House
Aykley Heads
Durham
DH1 5TS

Accounts Committee
Gateshead Council
Civic Centre
Regent Street
Gateshead
NE8 1HH

April 2020

Dear Members

Audit Strategy Memorandum – Year ending 31 March 2020

We are pleased to present our Audit Strategy Memorandum for Gateshead Council and Group (Council and Group) for the year ending 31 March 2020.

The purpose of this document is to summarise our audit approach, highlight significant audit risks and areas of key judgements and provide you with the details of our audit team. As it is a fundamental requirement that an auditor is, and is seen to be, independent of its clients, Section 7 of this document also summarises our considerations and conclusions on our independence as auditors.

We consider two-way communication with you to be key to a successful audit and important in:

- reaching a mutual understanding of the scope of the audit and the responsibilities of each of us;
- sharing information to assist each of us to fulfil our respective responsibilities;
- providing you with constructive observations arising from the audit process; and
- ensuring that we, as external auditors, gain an understanding of your attitude and views in respect of the internal and external operational, financial, compliance and other risks facing the Council and Group which may affect the audit, including the likelihood of those risks materialising and how they are monitored and managed.

This document, which has been prepared following our initial planning discussions with management, is the basis for discussion of our audit approach, and any questions or input you may have on our approach or role as auditor.

This document also contains specific appendices that outline our key communications with you during the course of the audit, and forthcoming accounting issues and other issues that may be of interest.

Client service is extremely important to us and we strive to continuously provide technical excellence with the highest level of service quality, together with continuous improvement to exceed your expectations so, if you have any concerns or comments about this document or audit approach, please contact me on 0781 375 2053.

Yours faithfully

Signed: {{_es_:signer1:signature }}

Cameron Waddell, Partner

For and on behalf of Mazars LLP

1. ENGAGEMENT AND RESPONSIBILITIES SUMMARY

Overview of engagement

We are appointed to perform the external audit of the Council and Group for the year to 31 March 2020. The scope of our engagement is set out in the Statement of Responsibilities of Auditors and Audited Bodies, issued by Public Sector Audit Appointments Ltd (PSAA) available from the PSAA website: https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/

Our responsibilities

Our responsibilities are principally derived from the Local Audit and Accountability Act 2014 (the 2014 Act) and the Code of Audit Practice issued by the National Audit Office (NAO), as outlined below:

Audit opinion

We are responsible for forming and expressing an opinion on the financial statements.

Our audit is planned and performed so to provide reasonable assurance that the financial statements are free from material error and give a true and fair view of the financial performance and position of the Council and Group for the year.

Value for Money

We are required to conclude whether of the Council and Group has proper arrangements in place to secure economy, efficiency and effectiveness in it its use of resources. We discuss our approach to Value for Money work further in section 5 of this report.

Reporting to the NAO

We report to the NAO on the consistency of the Council and Group financial statements with its Whole of Government Accounts (WGA) submission.

Electors' rights

The 2014 Act requires us to give an elector, or any representative of the elector, the opportunity to question us about the accounting records of the Council and Group and consider any objection made to the accounts. We also have a broad range of reporting responsibilities and powers that are unique to the audit of local authorities in the United Kingdom.

Our audit does not relieve management or Those Charged with Governance, of their responsibilities. The responsibility for safeguarding assets and for the prevention and detection of fraud, error and non-compliance with law or regulations rests with both Those Charged with Governance and management. In accordance with International Standards on Auditing (UK), we plan and perform our audit so as to obtain reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error. However our audit should not be relied upon to identify all such misstatements.

As part of our audit procedures in relation to fraud we are required to enquire of Those Charged with Governance as to their knowledge of instances of fraud, the risk of fraud and their views on management controls that mitigate the fraud risks.

The Council and Group is required to prepare its financial statements on a going concern basis by the Code of Practice on Local Authority Accounting. As auditors, we are required to consider the appropriateness of the use of the going concern assumption in the preparation of the financial statements and the adequacy of disclosures made.

For the purpose of our audit, we have identified the Accounts Committee as Those Charged with Governance.

2. YOUR AUDIT ENGAGEMENT TEAM

- Cameron Waddell, Partner
- cameron.Waddell@mazars.co.uk
- 0781 375 2053

- Jim Dafter, Senior Manager
- jim.dafter@mazars.co.uk
- 0781 587 6042

- Elaine Hall, Assistant Manager
- Elaine.hall@mazars.co.uk
- 07881 283350

In addition, as outlined in our engagement letter, an engagement control reviewer (EQCR) has been appointed for this engagement.

3. AUDIT SCOPE, APPROACH AND TIMELINE

Audit scope

Our audit approach is designed to provide an audit that complies with all professional requirements.

Our audit of the financial statements will be conducted in accordance with International Standards on Auditing (UK), relevant ethical and professional standards, our own audit approach and in accordance with the terms of our engagement. Our work is focused on those aspects of your business which we consider to have a higher risk of material misstatement, such as those affected by management judgement and estimation, application of new accounting standards, changes of accounting policy, changes to operations or areas which have been found to contain material errors in the past.

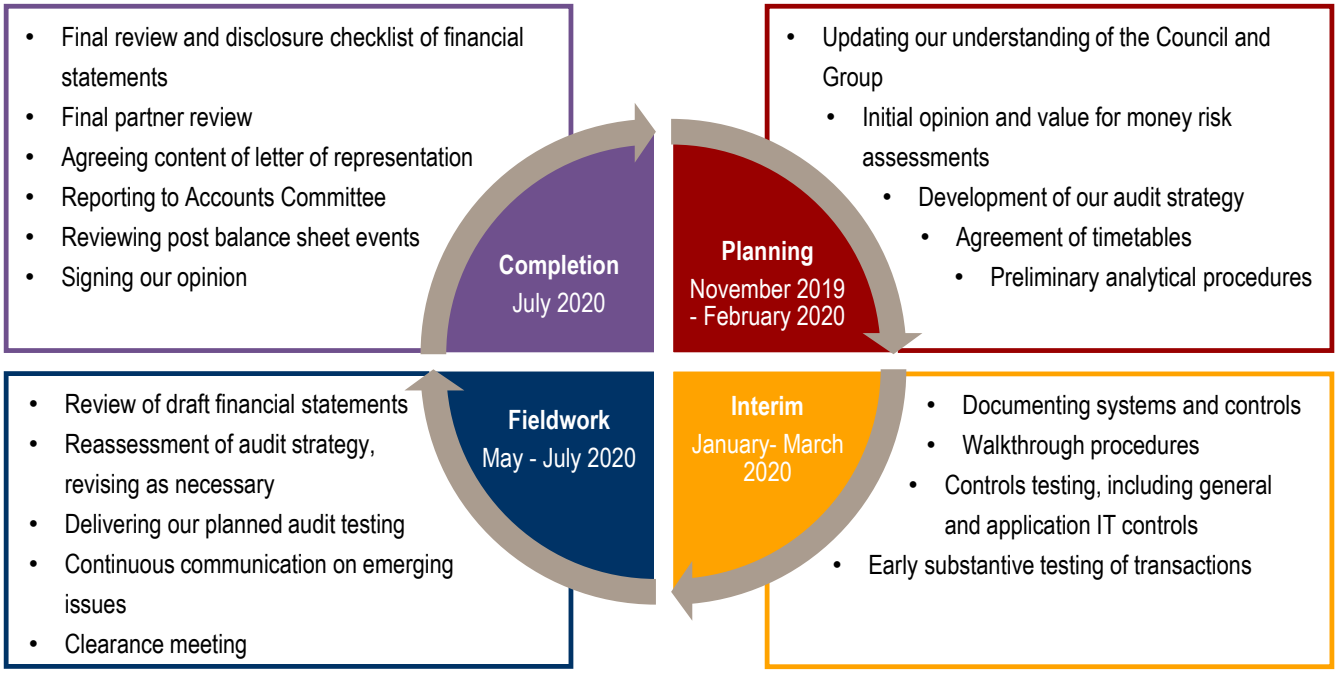
Audit approach

Our audit approach is a risk-based approach primarily driven by the risks we consider to result in a higher risk of material misstatement of the financial statements. Once we have completed our risk assessment, we develop our audit strategy and design audit procedures in response to this assessment.

If we conclude that appropriately-designed controls are in place then we may plan to test and rely upon these controls. If we decide controls are not appropriately designed, or we decide it would be more efficient to do so, we may take a wholly substantive approach to our audit testing. Substantive procedures are audit procedures designed to detect material misstatements at the assertion level and comprise tests of details (of classes of transactions, account balances, and disclosures) and substantive analytical procedures. Irrespective of the assessed risks of material misstatement, which take into account our evaluation of the operating effectiveness of controls, we are required to design and perform substantive procedures for each material class of transactions, account balance, and disclosure.

Our audit will be planned and performed so as to provide reasonable assurance that the financial statements are free from material misstatement and give a true and fair view. The concept of materiality and how we define a misstatement is explained in more detail in section 8.

The diagram below outlines the procedures we perform at the different stages of the audit.



3. AUDIT SCOPE, APPROACH AND TIMELINE (CONTINUED)

Reliance on internal audit

Where possible we will seek to utilise the work performed by internal audit to modify the nature, extent and timing of our audit procedures. We will meet with internal audit to discuss the progress and findings of their work prior to the commencement of our controls evaluation procedures.

Where we intend to rely on the work of internal audit, we will evaluate the work performed by your internal audit team and perform our own audit procedures to determine its adequacy for our audit.

Management's and our experts

Management makes use of experts in specific areas when preparing the Group's financial statements. We also use experts to assist us to obtain sufficient appropriate audit evidence on specific items of account.

Items of account	Management's expert	Our expert
Defined benefit liability	AON Hewitt Limited for Local Government Scheme	National Audit Office (NAO), prepared by PwC.
Property, plant and equipment valuations	BNP Paribas Real Estate (UK).	NAO's consulting valuer (Gerald Eve).
Financial instrument disclosures	Link Asset Services	Not required

Group audit approach

In line with the requirements of the CIPFA Code of Practice on Local Authority Accounting ('the Code'), officers have considered the Council's interests in other entities and determined that it will prepare group accounts which will consolidate The Gateshead Housing Company.

Component	Nature of component/ownership	Auditor
Gateshead Council	Parent – local authority	Mazars LLP
The Gateshead Housing Company	Subsidiary 100% owned by the Council. The principal activity of the Company is the day to day management, maintenance and improvement of the housing stock of the Council.	KPMG LLP

We assess the significance of the components as part of determining the level of work required. In assessing the significance of components, we consider a range of quantitative and qualitative factors including:

- whether any component exceeds a minimum of 15% of key benchmarks (revenues, expenditure, profit/loss before tax, total assets, net assets/liabilities);

3. AUDIT SCOPE, APPROACH AND TIMELINE (CONTINUED)

Group audit approach (continued)

- whether any financial statement area (FSA) is greater than 15% of the relevant FSA in the consolidated accounts and greater than performance materiality – this change, as a result of the EU audit directive, results in such components being classed as 'material but not significant' components which are however required to be subject to a group audit scope consistent with a significant component; and
- whether there are any risks of material misstatement in the components likely to result in material misstatement in the group financial statements.

Our assessment is summarised in the table below. Overall we have assessed that there are two significant components.

Component	Significant in terms of benchmarks?	Risks of material misstatement?	Commentary
The Council	Yes	Yes	Being the ultimate parent.
The Gateshead Housing Company (TGHC)	No	yes	material transactions and balances exist in relation to pensions.

Nature and scope of planned work

The table below sets out the estimated proportion of each component, relative to the overall group, as well as the nature and scope of planned work. Note that these are estimates and may be subject to change. The work described below is in addition to our review of group-wide controls and the consolidation process. The objective of the analytical procedures is to critically corroborate the group engagement team's conclusions that there are no significant risks of material misstatement of the aggregated financial information of components that are not significant components.

Component	% of total group revenues	% audited by Mazars	Nature of work	Scope of work
The Council	99.7%	100%	Parent – audited by Mazars.	Not applicable - parent
The Gateshead Housing Company (TGHC)	0.3%	0%	Group analytical procedures. Review of work undertaken by auditors of TGHC in relation to pensions.	Critical evaluation of the group engagement team's conclusion that there are no significant risks of material misstatement of the aggregated financial information of TGHC.
	100%	100%		

4. SIGNIFICANT RISKS AND KEY JUDGEMENT AREAS

Following the risk assessment approach discussed in section 3 of this document, we have identified relevant risks to the audit of financial statements. The risks that we identify are categorised as significant, enhanced or standard, as defined below:

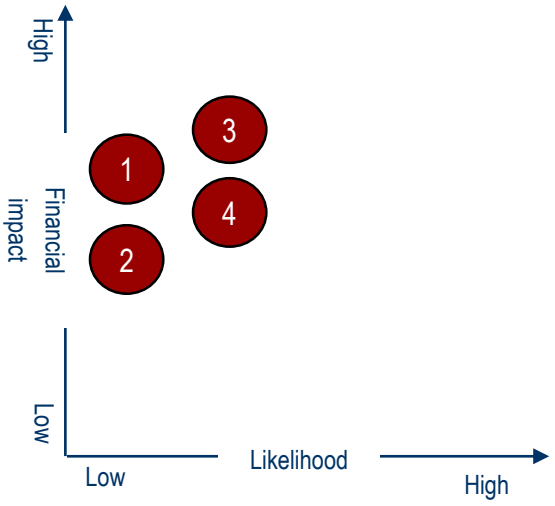
Significant risk A significant risk is an identified and assessed risk of material misstatement that, in the auditor's judgment, requires special audit consideration. For any significant risk, the auditor shall obtain an understanding of the entity's controls, including control activities relevant to that risk.

Enhanced risk An enhanced risk is an area of higher assessed risk of material misstatement at audit assertion level other than a significant risk. Enhanced risks incorporate but may not be limited to:

- key areas of management judgement, including accounting estimates which are material but are not considered to give rise to a significant risk of material misstatement; and
- other audit assertion risks arising from significant events or transactions that occurred during the period.

Standard risk This is related to relatively routine, non-complex transactions that tend to be subject to systematic processing and require little management judgement. Although it is considered that there is a risk of material misstatement, there are no elevated or special factors related to the nature, the likely magnitude of the potential misstatements or the likelihood of the risk occurring.

The summary risk assessment, illustrated in the table below, highlights those risks which we deem to be significant. We have summarised our audit response to these risks on the next page.



	Risk
1	Management override of control
2	Revenue recognition (miscellaneous income only) for Council only
3	Defined benefit liability valuation
4	Property, plant and equipment valuation for Council only

4. SIGNIFICANT RISKS AND KEY JUDGEMENT AREAS (CONTINUED)

We provide more detail on the identified risks and our testing approach with respect to significant risks in the table below. An audit is a dynamic process, should we change our view of risk or approach to address the identified risks during the course of our audit, we will report this to the Accounts Committee.

Significant risks

	Description of risk	Planned response
1	**Management override of controls** Management at various levels within an organisation are in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. Due to the unpredictable way in which such override could occur there is a risk of material misstatement due to fraud on all audits.	We plan to address the management override of controls risk through performing audit work over accounting estimates, journal entries and significant transactions outside the normal course of business or otherwise unusual.
2	**Revenue recognition (relevant to the Council)** Our audit methodology incorporates this risk as a significant risk at all audits, although based on the circumstances of each audit, it is rebuttable. We have concluded that we can rebut the presumption of a revenue recognition risk for the majority of the Council's revenue streams, consisting largely of taxation, business rates and grant income. However, we do not feel that sufficient scope exists to rebut this risk in respect of the recognition of fees, charges and other income given the demand led nature of these revenue streams . This does not imply that we suspect actual or intended manipulation but that we continue to deliver our audit work with appropriate professional scepticism. .	We will: • substantively test fees, charges and other income to ensure it has been correctly classified and recognised; • test journals; and • obtain direct confirmation of year-end bank balances and test the reconciliations to the ledger.
3	**Defined benefit liability valuation** The financial statements contain material pension entries in respect of retirement benefits. The calculation of these pension figures, both assets and liabilities, can be subject to significant volatility and includes estimates based upon a complex interaction of actuarial assumptions. This results in an increased risk of material misstatement.	We will discuss with key contacts any significant changes to the pension estimates. In addition to our standard programme of work in this area, we will evaluate the management controls you have in place to assess the reasonableness of the figures provided by the Actuary and consider the reasonableness of the Actuary's output, referring to an expert's report on all actuaries nationally which is carried out annually by the NAO's consulting actuary (PWC).

4. SIGNIFICANT RISKS AND KEY JUDGEMENT AREAS (CONTINUED)

	Description of risk	Planned response
4	**Property, plant and equipment – valuation (relevant to the Council)** The financial statements contain material entries on the Balance Sheet as well as material disclosure notes in relation to the Council's holding of PPE. Although the Council employs an external valuation expert to provide information on valuations, there remains a high degree of estimation uncertainty associated with the revaluation of PPE due to the significant judgements and number of variables involved in providing revaluations. We have therefore identified the revaluation of PPE to be an area of risk.	We will consider the Council's arrangements for ensuring that PPE values are reasonable and will use an external expert (Gerald Eve) to provide data to enable us to assess the reasonableness of the valuations provided by the Council's valuer. We will also assess the competence, skills and experience of the valuer. Where necessary we will also perform further audit procedures on individual assets to ensure that the basis and level of revaluation is appropriate.

Key areas of management judgement

Key areas of management judgement include accounting estimates which are material but are not considered to give rise to a significant risk of material misstatement. These areas of management judgement represent other areas of audit emphasis.

We have not identified any key areas of management judgement as part of our audit planning.

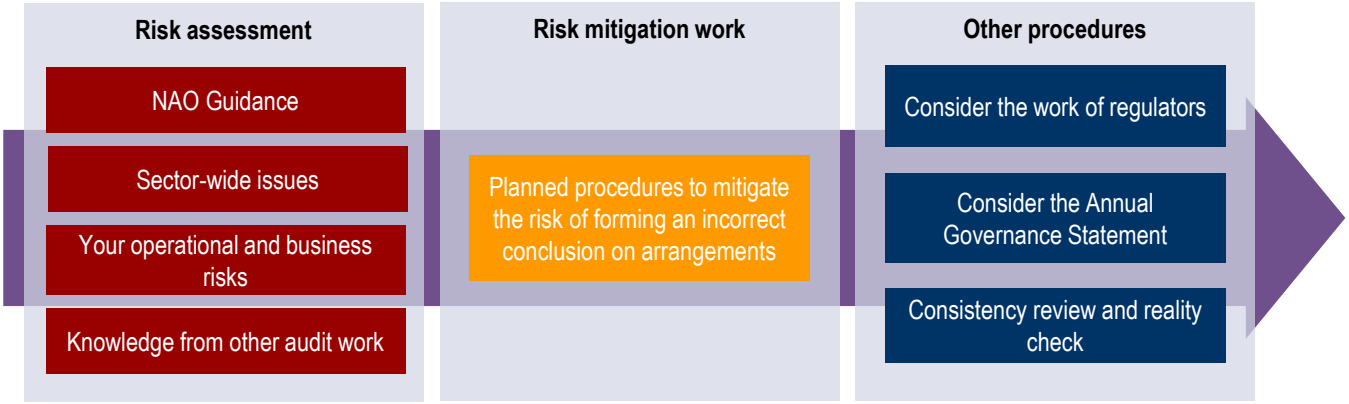
5. VALUE FOR MONEY

Our approach to Value for Money
We are required to form a conclusion as to whether the Council and Group has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The NAO issues guidance to auditors that underpins the work we are required to carry out, and sets out the overall criterion and sub-criteria that we are required to consider.

The overall criterion is that, 'in all significant respects, the Group had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.'

To assist auditors in reaching a conclusion on this overall criterion, the following sub-criteria are set out by the NAO:
- informed decision making;
- sustainable resource deployment; and
- working with partners and other third parties.

A summary of the work we undertake to reach our conclusion is provided below:



Significant Value for Money risks
The NAO's guidance requires us to carry out work at the planning stage to identify whether or not a Value for Money (VFM) exists. Risk, in the context of our VFM work, is the risk that we come to an incorrect conclusion rather than the risk of the arrangements in place at the Group being inadequate. As outlined above, we draw on our deep understanding of the Council and its partners, the local and national economy and wider knowledge of the public sector.

For the 2019/20 financial year, we have identified the following significant risk to our VFM work:

Description of significant risk	Planned response
Sustainable resource deployment Planning finances effectively to support the sustainable delivery of strategic priorities and maintain statutory functions The Council continues to face financial pressures from reduced funding, increased demand and changing responsibilities. The Council is responding to the challenges with a programme of efficiencies, service reviews and developing new ways to manage demand and deliver services. Failure to have appropriate arrangements in place to identify and deliver this programme poses a significant risk to the Council's ability to deliver its strategic priorities and maintain statutory functions.	We will review: • monitoring and action plans for a sample of savings included in the budget; • the updated Medium-Term Financial Strategy; • budget monitoring reports and other finance updates; and • the progress made in identifying further savings required;

6. FEES FOR AUDIT AND OTHER SERVICES

Fees for work as the Council's appointed auditor

We communicated our proposed fee of £100,329 in our fee letter dated 17 April 2019, which was in line with the scale fee set by PSAA. In 2018/19, the Council also prepared group financial statements alongside the Council's financial statements, as referenced in section 3 of this Memorandum, and we agreed a fee variation with the Council which was approved by PSAA for this additional audit work. Group accounts will continue to be produced in 2019/20, so this variation will again be required. We will write to PSAA in due course seeking approval of this variation for 2019/20.

In common with all local government external auditors we are required to carry out additional procedures which were not expected when fees were set.

Regulatory recommendations

We continually strive to maintain high standards of audit quality. One mechanism for doing this is to consider the outcome of independent quality reviews, in particular by the Financial Reporting Council, of our audit work and that of other audit suppliers. In particular we are planning increases in the level of work we do on:

- defined benefit pension schemes; and
- valuation of property, plant and equipment.

We will discuss the driving factors with Council officers and the audit fee for 2019/20 will be revisited to reflect the increased level of work that was not considered when the scale fee was set. Any agreed additional fee is also subject to detailed scrutiny by the PSAA as part of the approval process.

Service	2018/19 fee	2019/20 fee
Code audit work	£100,329	£100,329
Plus; additional fees in respect of audit of group consolidation	£9,724	£9,724
Total fees for Code audit work	**£110,053**	**£110,053***
Plus; Additional work in response to regulatory recommendations to increase level of audit work on the valuation of property plant and equipment.	**n/a**	To be agreed
Plus; Additional work in response to regulatory recommendations to increase level of audit work on defined benefit liability schemes.	**n/a**	To be agreed

* Subject to agreement by PSAA and confirmation from PSAA of 2019/20 scale rates for additional work.

All fees shown above are subject to VAT

6. FEES FOR AUDIT AND OTHER SERVICES

Fees for non-PSAA work

In addition to the fees outlined above in relation to our appointment by PSAA, we have been separately engaged by the Council to carry out additional work as set out in the table below. Before agreeing to undertake any additional work we consider whether there are any actual, potential or perceived threats to our independence. Further information about our responsibilities in relation to independence is provided in section 7.

Service	2018/19 fee	2019/20 fee
Assurance services: Housing Benefits Subsidy	£10,000 plus VAT	To be agreed
Assurance services: Teachers' Pensions	£3,750 plus VAT	To be agreed
Assurance services: Pooling of Housing Capital Receipts return	£2,200 plus VAT	To be agreed

7. OUR COMMITMENT TO INDEPENDENCE

We are committed to independence and are required by the Financial Reporting Council to confirm to you at least annually, in writing, that we comply with the Financial Reporting Council's Ethical Standard. In addition, we communicate any matters or relationship which we believe may have a bearing on our independence or the objectivity of the audit team.

Based on the information provided by you and our own internal procedures to safeguard our independence as auditors, we confirm that in our professional judgement there are no relationships between us and any of our related or subsidiary entities, and you and your related entities creating any unacceptable threats to our independence within the regulatory or professional requirements governing us as your auditors.

We have policies and procedures in place which are designed to ensure that we carry out our work with integrity, objectivity and independence. These policies include:

- all partners and staff are required to complete an annual independence declaration;
- all new partners and staff are required to complete an independence confirmation and also complete computer-based ethics training;
- rotation policies covering audit engagement partners and other key members of the audit team;
- use by managers and partners of our client and engagement acceptance system which requires all non-audit services to be approved in advance by the audit engagement partner.

We confirm, as at the date of this document, that the engagement team and others in the firm as appropriate, and Mazars LLP are independent and comply with relevant ethical requirements. However, if at any time you have concerns or questions about our integrity, objectivity or independence please discuss these with Cameron Waddell in the first instance.

Prior to the provision of any non-audit services Cameron Waddell will undertake appropriate procedures to consider and fully assess the impact that providing the service may have on our auditor independence. Included in this assessment is consideration of Auditor Guidance Note 01 as issued by the NAO, and the PSAA Terms of Appointment.

Any emerging independence threats and associated identified safeguards will be communicated in our Audit Completion Report.

Our assessment of perceived threats and safeguards for non-audit services in respect of 2019/20, as detailed in section 6, is set out in the table overleaf.

No threats to our independence have been identified.

Area of work	Perceived threat	Safeguards and commentary
Assurance Services: Housing Benefits Subsidy return	Self-review threat	No safeguards required. The fee for this work is neither significant to Mazars LLP nor the Council and Group and work undertaken will not be relied upon by the audit team.
Assurance Services: Pooling of Housing Capital Receipts return	Self-review threat	No safeguards required. The fee for this work is neither significant to Mazars LLP nor the Council and Group
Assurance Services: Teachers' Pensions Return	Self-review threat	No safeguards required. The fee for this work is neither significant to Mazars LLP nor the Council and Group

8. MATERIALITY AND MISSTATEMENTS

Summary of initial materiality thresholds

Threshold	Initial threshold - Council (£'000s)	Initial threshold - Group (£'000s)
Overall materiality	14,173	14,274
Performance materiality	10,630	10,706
Specific materiality:		
• Members allowances	10% of total amount disclosed	10% of total amount disclosed
• Termination benefits/exit packages	10% of total amount disclosed	10% of total amount disclosed
• Senior employees remuneration	100%	100%
Trivial threshold for errors to be reported to the Audit Committee	425	428

Materiality

Materiality is an expression of the relative significance or importance of a particular matter in the context of financial statements as a whole. Misstatements in financial statements are considered to be material if they, individually or in aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Judgements on materiality are made in light of surrounding circumstances and are affected by the size and nature of a misstatement, or a combination of both. Judgements about materiality are based on consideration of the common financial information needs of users as a group and not on specific individual users.

The assessment of what is material is a matter of professional judgement and is affected by our perception of the financial information needs of the users of the financial statements. In making our assessment we assume that users:

- have a reasonable knowledge of business, economic activities and accounts;
- have a willingness to study the information in the financial statements with reasonable diligence;
- understand that financial statements are prepared, presented and audited to levels of materiality;
- recognise the uncertainties inherent in the measurement of amounts based on the use of estimates, judgement and the consideration of future events; and
- will make reasonable economic decisions on the basis of the information in the financial statements.

We consider materiality whilst planning and performing our audit based on quantitative and qualitative factors.

Whilst planning, we make judgements about the size of misstatements which we consider to be material and which provides a basis for determining the nature, timing and extent of risk assessment procedures, identifying and assessing the risk of material misstatement and determining the nature, timing and extent of further audit procedures.

The materiality determined at the planning stage does not necessarily establish an amount below which uncorrected misstatements, either individually or in aggregate, will be considered as immaterial.

We revise materiality for the financial statements as our audit progresses should we become aware of information that would have caused us to determine a different amount had we been aware of that information at the planning stage.

8. MATERIALITY AND MISSTATEMENTS (CONTINUED)

Our provisional materiality is set based on a benchmark of gross expenditure at the surplus/deficit on provision of services level. We will identify a figure for materiality but identify separate levels for procedures designed to detect individual errors, and also a level above which all identified errors will be reported to the Audit Committee.

We consider that gross expenditure at the surplus/deficit on provision of services level remains the key focus of users of the financial statements and, as such, we base our materiality levels around this benchmark.

We expect to set a materiality threshold at 2% of gross revenue expenditure.

Based on last year's audited financial statements, we anticipate the overall materiality for the year ending 31 March 2020 to be in the region of £14.173 million for the Council (£14.173 million in the prior year) and £14.274 million for the Group (£14.274 million in the prior year).

After setting initial materiality, we continue to monitor materiality throughout the audit to ensure that it is set at an appropriate level.

Performance Materiality
Performance materiality is the amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce, to an appropriately low level, the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole.

Our initial assessment of performance materiality is based on low inherent risk, meaning that we have calculated performance materiality as being 75% of overall materiality. As with overall materiality, we will remain aware of the need to change this performance materiality level through the audit to ensure it remains to be set at an appropriate level.

Misstatements
We aggregate misstatements identified during the audit that are other than clearly trivial. We set a level of triviality for individual errors identified (a reporting threshold) for reporting to the Audit Committee that is consistent with the level of triviality that we consider would not need to be accumulated because we expect that the accumulation of such amounts would not have a material effect on the financial statements. Based on our preliminary assessment of overall materiality, our proposed triviality threshold is £425,000 (the Council) and £428,000 (Group) based on 3% of overall materiality. If you have any queries about this please do not hesitate to raise these with Cameron Waddell.

Reporting to the Audit Committee
To comply with International Standards on Auditing (UK), the following three types of audit differences will be presented to the Audit Committee:

- summary of adjusted audit differences;
- summary of unadjusted audit differences; and
- summary of disclosure differences (adjusted and unadjusted).

APPENDIX A – KEY COMMUNICATION POINTS

ISA (UK) 260 'Communication with Those Charged with Governance', ISA (UK) 265 'Communicating Deficiencies In Internal Control To Those Charged With Governance And Management' and other ISAs (UK) specifically require us to communicate the following:

Required communication	Audit Strategy Memorandum	Audit Completion Report
Our responsibilities in relation to the audit of the financial statements and our wider responsibilities	✓	
Planned scope and timing of the audit	✓	
Significant audit risks and areas of management judgement	✓	
Our commitment to independence	✓	✓
Responsibilities for preventing and detecting errors	✓	
Materiality and misstatements	✓	✓
Fees for audit and other services	✓	
Significant deficiencies in internal control		✓
Significant findings from the audit		✓
Significant matters discussed with management		✓
Our conclusions on the significant audit risks and areas of management judgement		✓
Summary of misstatements		✓
Management representation letter		✓
Our proposed draft audit report		✓

APPENDIX B – FORTHCOMING ACCOUNTING AND OTHER ISSUES

Financial reporting changes relevant to 2019/20

There are no significant changes in the Code of Practice on Local Authority Accounting for the 2019/20 financial year.

Financial reporting changes in future years

Accounting standard	Year of application	Commentary
IFRS 16 – Leases	2020/21	The CIPFA/LASAAC Code Board has determined that the Code of Practice on Local Authority Accounting will adopt the principles of IFRS 16 Leases, for the first time from 2020/21. IFRS 16 will replace the existing leasing standard, IAS 17, and will introduce significant changes to the way bodies account for leases, which will have substantial implications for the majority of public sector bodies. The most significant changes will be in respect of lessee accounting (i.e. where a body leases property or equipment from another entity). The existing distinction between operating and finance leases will be removed and instead, the new standard will require a right of use asset and an associated lease liability to be recognised on the lessee's Balance Sheet. In order to meet the requirements of IFRS 16, all local authorities will need to undertake a significant project that is likely to be time-consuming and potentially complex. There will also be consequential impacts upon capital financing arrangements at many authorities which will need to be identified and addressed at an early stage of the project.

APPENDIX C – MAZARS' CLIENT SERVICE COMMITMENT

We are here because of our clients; serving them in the best way we can is part of our DNA. We operate a Code of Conduct which drives our client service commitment in all areas, as set out below.

Gateshead Council

Audit and Standards Committee
9 March 2020

Title of Report: **Annual Governance Statement 2019/20 - Assurance Framework**

Report of: **Darren Collins, Strategic Director, Resources & Digital**

Purpose of the Report

1 This report provides an overview of the work to be undertaken to produce the Annual Governance Statement (AGS) for 2019/20 which demonstrates the level of assurance that can be given by the Council's control systems and governance arrangements.

Background

2 The Council is responsible for ensuring that its business is conducted in accordance with the law and proper standards and that public money is safeguarded, properly accounted for and used economically, efficiently and effectively demonstrating value for money.

3 The Accounts and Audit Regulations 2015 require the Council to produce an AGS setting out its governance arrangements and reviewing their effectiveness. The statement accompanies the Annual Statement of Accounts and is signed by the Leader of the Council and Chief Executive.

4 The overall aim is to ensure that resources are directed in accordance with agreed policy and according to priorities, that there is sound and inclusive decision making, that there is clear accountability for the use of those resources in order to achieve the desired outcomes for service users and the community.

Assurance Framework

5 The assurance framework supports the AGS and provides councillors with information on the Council's control environment and governance arrangements. It maps the Council's strategic objectives to risks and controls and seeks assurance from a number of sources of Council activity.

6 The process of preparing the AGS should itself add value to the effectiveness of the Governance Assurance Framework. The assurance process will demonstrate four aspects:

- **Identify** – what do we want assurance on?
- **Assess** – what are the sources of assurance?

- **Review** – how is assurance validated?
- **Act** – what are the opportunities to improve?

7 In preparing the governance statement it will be necessary to review evidence from the following sources which together form the assurance framework:

- Governance arrangements
- Councillors
- Senior Managers
- The system of internal audit
- Risk management arrangements
- Counter Fraud arrangements
- Performance management and data quality
- Views of the external auditor and other external inspectorates.
- The legal and regulatory framework
- Financial controls
- Partnership arrangements and governance
- Other sources of assurance.

Governance arrangements

8 The Council has a Local Code of Governance, which was originally presented to the Audit and Standards Committees in April 2007. This was last updated and agreed by the Audit and Standards Committee on 27 January 2020. This Code defines how the Council complies with the principals of good governance as set out in the Local Code of Governance developed by CIPFA, Delivering Good Governance in Local Government: Framework. The principles of good governance in the framework are:

- Behaving with integrity
- Ensuring openness and comprehensive engagement
- Defining sustainable outcomes
- Determining interventions
- Developing capacity
- Managing risks and performance
- Implementing good practice in transparency

9 The effectiveness of the Council's governance arrangements will be considered through the assessment of the assurances below.

Councillors

10 The Council's Constitution sets out the role of the Cabinet as follows:

- To lead change and make recommendations for change to the Council, in consultation with a range of stakeholders;

- To ensure that the Council's priorities within the policy framework and budget are implemented, making decisions within the framework where appropriate;

- To monitor and implement the budget and policy framework through taking a lead role on Best Value and through co-ordination with the Overview and Scrutiny role;

- To provide a public face for specific issues.

11 Assurance will be sought from members of the Cabinet on the effectiveness they feel can be placed on the Council's corporate governance arrangements.

Senior Managers

12 All Service Directors will complete a self assessment assurance statement detailing the level of assurance they feel they can place on their key control and governance processes. This statement will be reviewed and updated for 2019/20 to ensure it remains focused on the key areas. The evidence used to complete these statements will be evaluated by Internal Audit as part of the 2020/21 plan.

The system of internal audit

13 The Accounts and Audit Regulations 2015 require all authorities to "conduct an annual review of the effectiveness of internal audit and for a committee of the body to consider its findings" and that this process should be part of the annual review of the effectiveness of the system of internal control, which results in the production of the Annual Governance Statement. Best Practice highlights that "internal audit", in this context, includes not only the Internal Audit Service but also the Audit and Standards Committee.

14 The review ensures the opinion of the Chief Internal Auditor given in the Internal Audit Annual Report can be relied upon as a key source of evidence in the Annual Governance Statement.

15 The Strategic Director, Resources & Digital has delegated responsibility to maintain an adequate internal audit of the Council's financial affairs as required by Section 151 of the Local Government Act 1972.

16 This review of the effectiveness of the system of Internal Audit for 2019/20 will be undertaken by the Council's Internal Control Group, which includes the Strategic Directors of Resources & Digital and Corporate Services & Governance. This review will be based upon:

- Self-assessment against Public Sector Internal Audit Standards (PSIAS);
- Self-assessment against the CIPFA Role of the Head of Internal Audit;
- Assessment of the effectiveness of the Audit and Standards Committee;
- Relevant performance information; and
- Where appropriate, reliance placed upon Internal Audit by the Council's external auditor.

17 The overall opinion of the Chief Internal Auditor based on the work undertaken by the Internal Audit & Risk Service and other providers during the year will be reported to the June Audit and Standards Committee in the Internal Audit Annual Report 2019/20.

Risk management arrangements

18 The Corporate Risk Management Policy identifies the roles and responsibilities of the following key groups:

- Councillors through the engagement of Cabinet and the Audit and Standards Committee;
- Chief Executive;
- Strategic Director, Resources & Digital;
- Strategic Directors;
- Service Directors;
- Service Managers;
- Internal Audit & Risk Service; and
- the Corporate Risk and Resilience Group (including Service Risk Co-ordinators)

19 The Policy has been updated to reflect organisational changes which have taken place since it was first adopted. The existing governance arrangements provide a means by which the effectiveness of the Policy can be monitored, thereby facilitating its ongoing development.

20 The Strategic Director, Resources & Digital prepares an annual report for the Audit and Standards Committee detailing the Council's risk management arrangements during the year and its findings. The report also includes a view on the effectiveness of the Council's risk management arrangements.

Counter Fraud Arrangements

21 The Council's Counter Fraud and Corruption Strategy clearly identifies the Council's Commitment to an effective approach to Counter Fraud and Corruption and outlines the principles the Council is committed to in preventing and reporting fraud and corruption.

22 Regular reports on any activity relating to this Strategy, and progress against the fraud plan, are provided to the Committee.

23 A Counter Fraud and Corruption Policy and Fraud Response Plan forms an important part of the Counter Fraud and Corruption Strategy by setting the tone, culture and expectations of the Council, as part of the corporate framework. The Policy outlines the Council's attitude to and position on, fraud and corruption and sets out responsibilities for its prevention and detection. It also communicates important deterrence messages to employees, Councillors, and third parties that fraudulent conduct will not be tolerated by the Council and that the stance against fraud is endorsed and supported at the most senior level.

24 The Fraud Response Plan details the Council's procedures for responding to any incidents of suspected fraud or corruption. The Plan sets out how suspicions should be raised and how investigations will be conducted and concluded.

25 An annual report will be provided to the Committee on performance against the Strategy and the effectiveness of the Strategy.

Views of the external auditor and other external inspectors

26 The external auditor issues an Annual Audit Letter to the Council, providing a review of the Council's value for money arrangements and reporting any significant issues arising from the audit of the Council's financial statements.

27 There are a number of other external inspectorates which may report on management or governance arrangements at the Council in the course of the year.

Performance management and data quality

28 The Council's corporate performance management framework (PMF) is a positive tool for employees, managers and councillors to use to take appropriate action, allocate resources and drive improvement.

29 The PMF is reviewed periodically to ensure it provides effective challenge and supports the continuous improvement of Council services. Following the adoption in 2018 of the Council's strategic approach Making Gateshead a Place Where Everyone Thrives, the suite of strategic indicators was reviewed, and a number of changes identified which were formally agreed by Cabinet in January 2019. In addition, a Local Index of Need has been developed which makes better use of local data to inform decision making and support the Thrive Agenda. The review of the PMF will continue throughout 2020 to ensure it reflects delivery of the Council's strategic priorities and how resources are allocated to maximise achievement.

30 Every six months, performance is reported to SMG Services and Performance, the relevant Overview and Scrutiny Committee and Cabinet.

31 In addition, Service Directors use this data, as well as management and operational data, to guide development of their service business plans and service improvements.

Legal and regulatory framework

32 Assurance will be sought from the Strategic Director, Corporate Services and Governance as the Monitoring Officer who has a legal duty to ensure the lawfulness and fairness of decision-making within the Council. Compliance with established policies, procedures, laws and regulations is ensured by the requirement in the Constitution to give the Chief Executive, the Monitoring Officer and the Chief Finance Officer the

opportunity to comment on every committee report submitted to a decision-making body.

Financial controls

33 Assurance will be sought from the Strategic Director, Resources & Digital who is designated as the responsible officer for the administration of the Council's financial affairs under section 151 of the Local Government Act 1972. This includes ensuring the lawfulness and financial prudence of decision-making; providing advice, particularly on financial impropriety, publicity and budget issues; giving financial information; and acting as the Council's money laundering reporting officer.

Partnership arrangements & governance

34 Another requirement is for each Service Director to review the partnerships their Service is connected with and record details within their business plan on an annual basis. As partners are key to the delivery of the Council's objectives assurance of their control and governance systems is required. The overall opinion on the effectiveness of such arrangements will be presented in an annual report to the Audit and Standards Committee.

Other sources of assurance

35 Other areas include anything not covered above which gives an opinion on the Council's internal control environment or governance arrangements.

Production of the Annual Governance Statement 2019/20

36 A corporate group, chaired by the Strategic Director, Resources & Digital will use the findings of the above sources of assurance to form a view on the adequacy of the Council's overall internal control and governance arrangements.

37 Using evidence from this assessment the Group will prepare the AGS for 2019/20 for approval by the Audit and Standards Committee in June 2020. This will then accompany the Statement of Accounts for 2019/20.

Recommendation

38 The Committee is asked to agree the Assurance Framework as set out in this report.

Contact: Craig Oakes – Ext. 3711

Gateshead Council

REPORT TO AUDIT AND STANDARDS COMMITTEE
9 MARCH 2020

Title of report: **Treasury Policy Statement and Treasury Strategy 2020/21 to 2024/25**

Report of: **Darren Collins – Strategic Director, Resources and Digital**

Purpose of the Report

1. This report asks the Audit and Standards Committee to review the proposed Treasury Policy Statement and Treasury Strategy for 2020/21 to 2024/25 prior to consideration by Cabinet.

Background

2. To provide a framework for the Strategic Director, Resources and Digital to exercise his delegated powers, the Council agrees a five-year Treasury Management Policy and Treasury Strategy which is reviewed at the start of each financial year.

3. The attached Treasury Policy and Treasury Strategy have been prepared considering the Local Government Act 2003, Ministry of Housing, Communities and Local Government 's (MHCLG) Guidance on Local Government Investments, CIPFA's Prudential Code for Capital and CIPFA's Code of Practice on Treasury Management (2017).

Proposals

4. The Committee is asked to review the Treasury Policy and Treasury Strategy attached at Appendix 2 and Appendix 3, to ensure that the Council fully complies with the requirements of good financial practice in Treasury Management.

Recommendation

5. The Committee is asked to review the recommendations on the Treasury Policy and the Treasury Strategy and submit any comments to Cabinet.

For the following reason:

- To ensure that the Council fully complies with the requirements of good practice as recommended by the Local Government Act 2003, the Chartered Institute of Public Finance and Accountancy (CIPFA) in its Code of Practice on Treasury Management and Prudential Code for Capital (2017) and the Ministry of Housing, Communities and Local Government (MHCLG), Guidance on Local Government Investments.

CONTACT: Clare Morton, ext. 3591

Policy Context

1. The proposals in this report are consistent with Council priorities and in particular they ensure that effective use is made of the Council's resources to ensure a sustainable financial position. The Council has approached the budget consultation for 2020 within a framework for achieving the Council's strategic approach 'Making Gateshead a Place Where Everyone Thrives'. The Council recognises there are huge financial pressures on not just council resources, but those of partners, local businesses and residents. To deliver on the strategic approach over the next five years, the Council will need to be resolute in its determination to make Gateshead a place where everyone thrives. This means the Council's decision-making will be policy and priority led and driven.

Background

2. The Prudential Code plays a key role in capital finance in local authorities. Local authorities determine their own programmes for capital investment that are central to the delivery of quality public services. The Prudential Code was developed by CIPFA, the Chartered Institute of Public Finance and Accountancy, as a professional code of practice to support local authorities in taking their decisions. Local authorities are required by regulation to have regard to the Prudential Code when carrying out their duties in England and Wales under Part 1 of the Local Government Act 2003.

3. In December 2017 CIPFA issued a revised Treasury Management Code of Practice and a revised Prudential Code (the Code) which represents best practice. The Council fully complies with the Code and this contributes towards achieving good practice.

4. Part 1 of the Local Government Act 2003 specifies the powers of a local authority to borrow for any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs. Borrowing is linked to the CIPFA Prudential Code for Capital which sets out a range of prudential and treasury indicators that must be calculated to ensure borrowing is affordable, prudent and sustainable. The Prudential Code refers to the need for a clear and integrated treasury strategy.

5. In addition, under Section 15 of the Local Government Act 2003, authorities are required to have regard to the MHCLG's guidance on Local Government Investments. This document stipulates the requirement for an annual investment strategy to be integrated into the Council's Treasury Strategy.

6. MHCLG introduced revised investment guidance which was effective for financial years commencing on or after 1st April 2018. The revised guidance focuses on non-financial asset investments, for example investment in commercial property.

7. Under Part 4 of the Council's Constitution the Strategic Director, Resources and Digital will produce a Treasury Policy Statement annually, setting out the general policies and objectives of the Council's treasury management function.

8. The Council also provides a treasury management service to the Gateshead Housing Company through a Service Level Agreement.

Treasury Policy

9. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on the risk implications for the Council.

10. The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

11. CIPFA's Treasury Management Code requires the setting out of responsibilities and duties of councillors and officers to allow a framework for reporting and decision making on all aspects of treasury management. To achieve this CIPFA has recommended the adoption of 13 treasury management practices (TMPs).

12. These principles are intended to provide a working document that forms a detailed framework for treasury management activities. The policy fully encompasses CIPFA's Code of Practice. In addition, the policy fully takes account of the requirements of the Prudential Code for Capital Finance in Local Authorities and the guidance issued by the MHCLG supporting Part 1 of the Local Government Act 2003 in respect of local authority investments. The Treasury Policy is attached at Appendix 2.

Treasury Strategy

13. The Treasury Strategy for 2020/21 to 2024/25 is attached at Appendix 3. This covers the specific activities proposed for 2020/21 to 2024/25 in relation to both borrowing and investments and ensures a wide range of advice is taken to maintain and preserve all principal sums, whilst obtaining a reasonable rate of return, and that the most appropriate borrowing is undertaken. The primary objective of the investment strategy is to maintain the security of investments at all times.

14. The term "investments" used in the definition of treasury management activities also covers non-financial assets which the Council may hold primarily for financial returns. The control of risk and optimising returns on these more commercial investments is consistent with the Council's risk appetite.

15. Under the requirements of the Prudential Code and Treasury Management Code of Practice the Council have adopted prudential indicators (detailed in Appendix 4). Details of investment types, minimum credit ratings, circumstances of use and maximum investment period are shown in Appendix 5.

16. The Council have reviewed the maximum maturity periods and amounts which can be invested with counterparties outlined in Appendix 6. In ensuring that these limits meet our requirements an assessment of risk has been undertaken and advice obtained from Link Asset Services.

17. The Council has produced the Treasury Strategy to comply with the requirements of the Code, the Prudential Code for Capital Finance in Local Authorities (2017) and Part 1 of the Local Government Act 2003. The Council considers that compliance with the above ensures that best practice is followed.

Consultation

18. Consultation on the production of the Treasury Policy Statement, including the Treasury Strategy for 2020/21 to 2024/25, has taken place with the Council's treasury advisers (Link Asset Services). The outcome of the consultation process, along with guidance issued by CIPFA and the MHCLG, has informed the format and content of the policy and strategy statements.

19. The Leader of the Council has been consulted on the contents of this report.

Alternative Options

20. There are no alternative options, as the Treasury Policy and Strategy reports recommended for approval are required in order to comply with CIPFA's Code of Practice on Treasury Management (2017). the Local Government Act 2003 and MHCLG Guidance on Local Government Investments.

Implications of recommended options

21. **Resources:**

a) **Financial Implications** - The Strategic Director, Resources and Digital, confirms that the financial implications are set out in this report. There are no additional financial implications associated with the report itself.

b) **Human Resources Implications** - There are no human resources implications arising from this report.

c) **Property Implications** – There are no property implications arising from this report.

22. **Risk Management Implications**

The Treasury Policy and Treasury Strategy which informs activity in this area were prepared with the primary aim of minimising risk to ensure that the Council's principal sums are safeguarded. Maximising income is considered secondary to this main aim.

23. **Equality and Diversity Implications**

There are no equality and diversity implications arising from this report.

24. **Crime and Disorder Implications**

There are no crime and disorder implications arising from this report.

25. **Sustainability Implications**

There are no sustainability implications arising from this report.

26. **Human Rights Implications**

There are no human rights implications arising from this report.

27. **Area and Ward Implications**

There are no direct area and ward implications arising from this report.

28. **Background Information:**

The following documents have been used in preparation of the report:

- Local Government Act 2003
- MHCLG Guidance on Local Government Investments
- CIPFA's Prudential Code for Capital (2017)
- CIPFA's Code of Practice on Treasury Management (2017)

Appendix 2

Treasury Policy 2020/21 to 2024/25

1. Approved Activities of the Treasury Management Operation

1.1 In December 2017 CIPFA published a revised Code of Practice on Treasury Management in the Public Services (the Code), which represents best practice. Treasury management activities are defined by CIPFA as:

> "The management of the organisation'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."

1.2 The term "investments" used in the definition of treasury management activities includes all financial assets of the organisation, as well as other non-financial assets which the Council may hold primarily for financial returns. The control of risk and optimising returns on these more commercial investments is also consistent with the Council's risk appetite.

1.3 The Council provides a treasury management service to the Gateshead Housing Company through a Service Level Agreement.

2. Formulation of the Treasury Strategy

2.1 The formulation of a Treasury Strategy involves determining the appropriate borrowing and investment decisions with the prime objective of safeguarding the Council's assets and secondary objectives of obtaining a reasonable rate of return on investments and minimising the costs of borrowing. Accordingly, the analysis and reporting of treasury management activities will focus on the risk implications for the Council and ensure robust due diligence procedures cover all treasury and non-treasury investments.

2.2 The Treasury Strategy encompasses the requirements of CIPFA's Treasury Management Code of Practice, Prudential Code for Capital and the MHCLG Guidance on Local Government Investments.

2.3 The Strategy for 2020/21 to 2024/25 is attached at Appendix 3.

3. Prudential and Treasury Indicators

3.1 Under Part 1 of the Local Government Act 2003 the Council may borrow money
(a) for any purpose relevant to its functions under any enactment, or
(b) for the purposes of the prudent management of its financial affairs.

3.2 Under the requirements of the Prudential Code and Treasury Management Code of Practice the Council have adopted prudential indicators (detailed in Appendix 3, section 1.4).

4. Annual Investment Strategy

4.1 The MHCLG has issued guidance to supplement the investment regulations contained within the Local Government Act 2003. It is also referred to under Section

15 (1) of the 2003 Local Government Act which requires authorities to “have regard (a) to such guidance as the Secretary of State may issue and (b) to such other guidance as the Secretary of State may by regulations specify”. The guidance encourages authorities to invest prudently but without burdening them with the detailed prescriptive regulation of the previous regime.

4.2 Central to the guidance and the Code is the need to produce an Annual Investment Strategy. This is included as Section 6 of the Treasury Strategy in Appendix 3.

4.3 The Annual Investment Strategy document will include:

- The Council’s risk appetite in respect of security, portfolio liquidity and return;
- The definition of ‘high’ and ‘non-high’ credit quality to determine what are specified investments and non-specified investments;
- Which specified and non-specified instruments the Council will use, dealing in more detail with non-specified investments given the greater potential risk;
- The categories of counterparties that may be used during the course of the year e.g. foreign banks, nationalised/part nationalised banks, building societies;
- The types of investments that may be used during the course of the year;
- The limit to the total amount that may be held in each investment type;
- The Council’s policy on the use of credit ratings, credit rating agencies and other credit risk analysis techniques to determine creditworthy counterparties for its approved lending list and how the Council will deal with changes in ratings, rating watches and rating outlooks;
- Limits for individual counterparties, groups and countries;
- Guidelines for making decisions on investments and borrowing; and
- The Council’s policy on commercial investments held for return.

5. Policy on Interest Rates Exposure

5.1 The use of any financial instruments, such as derivatives, to mitigate interest rate risks will be considered on an individual basis and the Strategic Director, Resources and Digital, will obtain approval from the Council prior to entering into any arrangement of this nature.

6. Policy on Delegation, Review Requirements and Reporting Arrangements

6.1 It is the Council’s responsibility under the Code to approve a Treasury Policy statement.

6.2 The Council delegates the review of the policy and monitoring of the performance of the treasury management function to Cabinet, the scrutiny of treasury management strategy and policies to the Audit and Standards Committee, and the execution and administration of treasury management decisions to the Strategic Director, Resources and Digital, who will act in accordance with the organisations policy statement and TMPs and CIPFA’s Standard of Professional Practice on Treasury Management. Any proposals to approve, adopt or amend policy require the consent of the Council and are matters for the Council to determine.

6.3 Treasury Strategy (Appendix 3, section 1.3) outlines the Councils arrangements for reporting on Treasury Management.

6.4 As from 1st April 2019, CIPFA required all local authorities to prepare an additional report, a Capital Strategy report, which is intended to provide the following: -

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

6.5 The aim of this report is to ensure that all elected members of the council fully understand the overall strategy, governance procedures and risk appetite entailed by this Strategy.

6.6 The Capital Strategy 2020/21 to 2024/25 was approved by Cabinet on 19th November 2019.

Appendix 3

Treasury Strategy 2020/21 to 2024/25

1. Introduction

1.1 The CIPFA Code of Practice on Treasury Management 2017 (the Code) emphasises a number of key areas including the following:

a) All authorities must formally adopt the Code.
b) The strategy report will affirm that the effective management and control of risk are prime objectives of the Council's treasury management activities.
c) The Council's appetite for risk, including the appetite for any use of financial instruments in the prudent management of those risks, must be clearly identified within the strategy report and will affirm that priority is given to security and portfolio liquidity when investing treasury management funds and explain how that will be carried out.
d) Responsibility for risk management and control lies within the organisation and cannot be delegated to any outside organisation.
e) Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support.
f) Councils need a sound diversification policy with high credit quality counterparties and should consider setting country, sector and group limits.
g) Borrowing in advance of need is only to be permissible when there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities.
h) The main annual treasury management reports must be approved by full Council.
i) There needs to be a mid-year review of Treasury Management Strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved.
j) Each council must delegate the role of scrutiny of Treasury Management Strategy and policies to a specific named body.
k) Treasury Management performance and policy setting should be subjected to prior scrutiny.
l) Councillors should be provided with access to relevant training as those charged with governance are also personally responsible for ensuring they have the necessary skills and training.
m) Responsibility for these activities must be clearly defined within the organisation.
n) Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Council (this will form part of the Treasury Management Practices).
o) "Investments" covers the financial and non-financial assets which the organisation holds primarily for financial returns. This will include investments which are not managed as part of the normal treasury management delegations.

1.2 This Strategy has been prepared in accordance with the Code.

1.3 The Council will adopt the following reporting arrangements in accordance with the requirements of the revised Code:

Area of Responsibility	**Council/ Committee/ Officer**	**Frequency**
Treasury Management Policy & Strategy / Annual Investment Strategy	Council approval with review delegated to Cabinet/ Audit and Standards Committee	Annually before the start of the year or where a material change is proposed
Annual Report on borrowing and investment activity	Council with review delegated to Cabinet/ Audit and Standards Committee	Annually by 30 September after the end of the year
Scrutiny of treasury management performance via mid-year report	Council approval with review delegated to Cabinet / Audit and Standards Committee	Mid-Year
In year changes to agreed Treasury Management Policy & Strategy / Annual Investment Strategy / Prudential and Treasury Indicators	Cabinet	By exception
Scrutiny of treasury management Policy, Strategy and procedures	Audit and Standards Committee	Annually before the start of the year
Treasury Management Monitoring Reports	Strategic Director, Resources and Digital	Bi-Monthly/Weekly
Treasury Management Practices	Strategic Director, Resources and Digital	Monthly

1.4 Given the link to the revenue budget and capital programme, the following indicators were approved by the Council on 27 February 2020 as part of the Budget and Council Tax Level 2020/21 report. For completeness, the approved indicators are attached at Appendix 4:

- Actual and estimates of financing costs to net revenue stream;
- Estimates of capital expenditure;
- Actual capital expenditure;
- Estimate of Capital Financing Requirement;
- Actual Capital Financing Requirement;
- Authorised limit;
- Operational boundary;
- Actual external debt;
- Gross debt and Capital Financing Requirement;
- Upper and lower limit of maturity structure of borrowing fixed and variable; and
- Upper limit on principal sums invested for periods of over 365 days.

1.5 In addition to the above indicators, local indicators showing the level of reserves which are backed by cash in the bank and internal borrowing as a percentage of the capital financing requirement are included in this report. Also, where there is a significant difference between the net and the gross borrowing position the risk and benefits associated with this strategy will be clearly stated in the annual strategy. This is highlighted within the main borrowing strategy outlined in section 4.6 below.

1.6 The strategy covers:

a) Prospects for interest rates;
b) Treasury limits in force which will limit the treasury risk and activities of the Council, including prudential and treasury indicators;
c) The borrowing strategy;
d) Sensitivity forecast;
e) External and internal borrowing;
f) Debt rescheduling;
g) Policy on borrowing in advance of need;
h) The investment strategy; and
i) The policy on the use of external service providers.

2. Prospects for Interest Rates

2.1 The table shown below outlines the Council's view of anticipated movements in interest rates, based on guidance received from the Council's treasury management advisers Link Asset Services as at 31January 2020.

	March 2020	June 2020	Sept 2020	Dec 2020	March 2021	March 2022	March 2023
Bank Rate	0.75%	0.75%	0.75%	0.75%	0.75%	1.00%	1.25%
5 yr PWLB*	2.30%	2.30%	2.40%	2.40%	2.50%	2.90%	3.10%
10 yr PWLB	2.50%	2.50%	2.60%	2.60%	2.70%	3.10%	3.30%
25 yr PWLB	3.00%	3.00%	3.10%	3.20%	3.30%	3.70%	3.90%
50 yr PWLB	2.90%	2.90%	3.00%	3.10%	3.20%	3.60%	3.80%

* Public Works Loan Board, a statutory body operating within the UK Debt Management Office, which is an executive agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities, and to collect the repayments.

Interest Rates

2.2 The Monetary Policy Committee (MPC) left Bank Rate unchanged at 0.75% at their meeting on 30th January 2020, with a vote of 7-2 for no change. The MPC suggested that there may still be a rate cut in the near future but only if inflation stays low.

The economic data releases since the election have shown some signs of improvement. However, should the positive signals not be sustained, including a rise in domestic price inflation, then the Bank of England are likely to act and cut rates. It should also be noted that if the economy recovers then there could be potential for modest interest rate hikes. The Gross Domestic Product forecast for 2020 was revised lower to 1.2% and in 2021 down to 1.4%. At market interest rate levels, the Bank of England feels that the 2% inflation target may only just be reached in two years' time, which seems to point to the need for a cut in rates, which will need to be maintained. MPC members agreed to make a reassessment of policy in March, by

which time they will know if recent data reflected a strengthening economy and whether the fiscal boost will eradicate the need to cut rates.

Long Term Interest Rates

2.3 Investment returns are likely to remain low during 2020/21 with little increase in the following two years. However, depending on progress with a Brexit trade deal, then there is potential for increases in investment interest earnings.

3 Treasury Limits for 2020/21 to 2024/25 including Prudential Indicators

3.1 It is a statutory requirement of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 31(a), as amended by the Localism Act 2011, requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from increases in interest charges and increases in running costs from new capital projects are limited to a level, which is affordable within the projected income of the Council for the foreseeable future. This is reported within the Council's Medium Term Financial Strategy.

3.2 It is a statutory duty under Section 3 of Part 1 of the Local Government Act 2003**,** and supporting regulations, for the Council to determine and keep under review how much it can afford to borrow. The amount so determined is termed the Affordable Borrowing Limit. The Authorised Limit represents the legislative limit specified in the Act.

3.3 The Prudential Code for Capital Finance in Local Authorities is a professional code that sets out a framework for self-regulation of capital spending, in effect allowing councils to invest in capital projects without any limit as long as they are affordable, prudent and sustainable. The Code requires that treasury management decisions be taken in accordance with good professional practice and in full understanding of the risks involved and how these risks will be managed to levels that are acceptable to the Council. The Council will take into account its arrangements for the repayment of debt and consideration of any impact, on the authority's overall fiscal sustainability.

3.4 The Council must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires the Council to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax and housing rent levels is affordable.

3.5 To facilitate the decision-making process and support capital investment decisions the Prudential Code and the Treasury Management Code require the Council to agree and monitor a minimum number of prudential indicators which were approved by Council on 27 February 2020 as attached at Appendix 4.

3.6 The Strategic Director, Resources and Digital, will ensure systems are in place to monitor the treasury limits and will report to Council instances where limits are breached, with the exception of short-term breaches of the Operational Boundary. The Operational Boundary is set so that if breached it acts as an early warning of the potential to exceed the higher Authorised Limit and as such temporary breaches due to debt restructuring and temporary borrowing are acceptable, providing they are not sustained.

4 Borrowing Strategy

4.1 The Local Government Act 2003 does not prescribe approved sources of finance, only that borrowing may not, without the consent of HM Treasury, be in other than Sterling.

4.2 The main options available for the borrowing strategy for 2020/21 are PWLB loans, market loans, capital market loans and the Municipal Bond Agency. The interest rate applicable to either PWLB or markets loans can be fixed or variable.

4.3 Variable rate short term borrowing is expected to be cheaper than long term fixed borrowing and therefore may be considered throughout the financial year. Due to the expectation that interest rates will rise, the risk of the potential increase in interest rates will be balanced against any potential short-term savings.

4.4 There are different types of market loans available, including forward starting, at variable and fixed interest rates. It is not usual practice to agree forward starting loans, but their use may be considered to avoid the 'cost of carry' – the difference between borrowing costs and investment returns. These loans generally would have to be offered at rates below the current or future PWLB forecast rates to make them an attractive option and considered as a means of mitigating future interest rate movements if the opportunity arose, i.e. where the Council can agree an interest rate ahead of when it would actually be required to draw down the funds.

4.5 To mitigate this interest rate risk a limit is placed on the total level of borrowing that can be taken as variable interest rate loans. To provide scope to utilise new market products should they become available as well as minimise the cost of borrowing and increase the diversification of the debt portfolio it is proposed that the limit on variable rate loans should be 40% of total borrowing in 2020/21.

4.6 The main strategy is therefore:

- Current (January 2020) long term PWLB rates (50 years) are around 2.75%. It is forecast that this will rise over the financial year 2020/21 with targets rates being, 2.90% Q1, 3.00% Q2, 3.10% Q3 and 3.20% Q4. Should interest rates fall below these targets borrowing should be considered, with preference given to terms which ensure a balanced profile of debt maturity, this may include Local Infrastructure Rate borrowing. The average interest rates forecast across this financial year for various borrowing periods are as follows: -
  10 years – 2.58%
  25 years – 3.12%
  50 years – 3.02%

- Whilst monitoring borrowing interest rates if there appears to be an upward trend then it may be considered prudent to lock into rates which exceed those outlined in paragraph 4.6 above, to minimise interest rate risk.

- The use of short-term borrowing (6 months to 18 months) will also be considered with the aim of minimising borrowing costs. This short-term borrowing will be replaced with longer term loans when rates are preferable.

- External borrowing rates currently far exceed the return that is available for investments, meaning savings can be achieved by borrowing internally from

reserves in the short term. The current policy of internal borrowing will continue to be followed as a short-term funding option serving to minimise overall cost.

- Consideration will be given to borrowing market loans which are at least 20 basis points below the PWLB target rate.

Sensitivity of the forecast

4.7 The Council, in conjunction with Link Asset Services, will continually monitor both the prevailing interest rates and the market forecasts, adopting the following responses to any changes. The main sensitivities of the forecast are likely to be the two scenarios below:

- *if it was felt that there was a significant risk of a sharp FALL in borrowing rates*, (e.g. due to a marked increase of risks around relapse into recession or of risks of deflation), then borrowing will be postponed, subject to availability of internal resources.

- *if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast*, perhaps arising from an acceleration in the rate of increase in central rates in the USA and UK, 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.

4.8 Against this background, caution will be adopted in the management of the 2020/21 treasury operations. The Strategic Director, Resources and Digital, will monitor the interest rate market and adopt a pragmatic approach to any changing circumstances having delegated powers to invest and manage the funds and monies of the Council.

External and Internal Borrowing

4.9 As at 30 November 2019 the Council had net debt of £595.921m; this includes total borrowing of £665.224m and investments of £69.303m.

4.10 Investment returns are likely to remain relatively low during 2020/21 but to be on a rising trend over the next few years.

4.11 Borrowing interest rates were falling during the first half of 2019-20 but were then increased by HM Treasury on 9th October 2019 by 100 bps. The policy of avoiding new borrowing by running down spare cash balances has served the Council well over recent years. However, this needs to be carefully reviewed to avoid incurring higher borrowing costs in the future when it may not be possible to avoid new borrowing to finance capital expenditure and/or refinance maturing debt.

4.12 There remains a cost of carry, (the difference between higher borrowing costs and lower investment returns) to any new long term borrowing that causes a temporary increase in cash balances as this position will most likely incur a revenue cost.

Borrowing in advance of need

4.13 The Council will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be considered carefully to ensure that it is in line with the projected

capital financing requirement and prudential indicators and that the Council can demonstrate value for money and ensure the security of the funds.

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

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow; and
- consider the alternative forms of funding.

Municipal Bond Agency

4.15 It is possible that the Municipal Bond Agency will be offering loans to local authorities in the future. The agency hopes that the borrowing rates will be lower than those offered by the Public Works Loan Board (PWLB). The Council may consider this as an additional source of borrowing as and when appropriate.

5. Debt Rescheduling

5.1 Any rescheduling opportunities will be considered in line with procedures approved under the Council's Treasury Management Practice Statements and will include a full cost/benefit analysis of any proposed variations. Any positions taken via rescheduling will be in accordance with the strategy position outlined in Section 4 above and will also take into account the prudential and treasury limits.

5.2 The reasons for any proposed rescheduling will include:

- the generation of cash savings at minimum risk;
- help to fulfil the treasury strategy; and
- in order to amend the maturity profile and/or the balance of volatility in the Council's borrowing portfolio.

5.3 The Strategic Director, Resources and Digital, in line with delegated powers outlined in the approved Treasury Management Practice Statement, will approve all rescheduling.

5.4 The Council has examined the potential for undertaking early repayment of external PWLB or LOBO debt in order to reduce the difference between its gross and net debt positions. The significant difference between early redemption rates and interest rates payable on new debt means that large premiums are likely to be incurred by such action. This situation will be monitored in case the differential is narrowed by changes in current borrowing rates.

5.5 Consideration will also be given to the potential for making savings by running down investment balances by repaying debt prematurely as short-term rates on investments are likely to be lower than rates paid on currently held debt. However, this will need careful consideration in the light of premiums that may be incurred by such a course of action and other financial considerations.

All rescheduling will be reported to Council in the mid-year and annual reports.

6. Investment Strategy 2020/21 to 2024/25

Introduction

6.1 The Council has regard to the MHCLG's Guidance on Local Government Investments and CIPFA's Code of Practice. The Council must produce a strategy on an annual basis which covers the subsequent five years.

6.2 The CIPFA definition of "investments" covers all the financial assets of the organisation, as well as other non-financial assets which the organisation holds primarily for financial returns, such as investment property portfolios. This may therefore include investments which are not managed as part of normal treasury management or under treasury management delegations.

6.3 This annual strategy states which investments the Council may use for the prudent management of its treasury balances during the financial year under the categories of **specified investments** and **non-specified investments.**

- Specified investments are those with a high-level credit quality and subject to a maturity limit of one year.
- Non-specified investments are those with less high credit quality, may be for periods in excess of one year and/or are more complex instruments which require greater consideration by members and officers before being authorised for use.

6.4 Both specified and non-specified investment types currently utilised by the Council are detailed in Appendix 6, along with approved limits. These limits reflect the Council's investment requirements whilst assessing risk and obtaining advice from Link Asset Services.

6.5 In addition to these, numerous other investment options are available for use and these may be considered suitable for use in the future. Should this be the case then the option will be evaluated in line with the procedures contained within the approved Treasury Management Practice Statement.

Investment Objectives

6.6 All investments will be in Sterling.

6.7 The Council's primary investment objective is the security of the capital investment. The Council will also manage the investments to meet cash flow demands and to achieve a reasonable return commensurate with the proper levels of security and liquidity. The risk appetite of the Council is low in order to give priority to security of its investments.

6.8 The borrowing of monies purely to invest is unlawful and the Council will not engage in such activity.

Creditworthiness Policy

6.9 The Council applies the creditworthiness service provided by Link Asset Services. The service uses a sophisticated modelling approach with credit ratings from the three main rating agencies - Fitch, Moody's and Standard and Poor's. This service uses a scoring system to ensure that it does not give undue consideration to just one

agency's ratings. It does not rely solely on the current credit ratings of counterparties but also uses the following information as overlays which are combined in a weighted scoring system:

- Credit watches and credit outlooks from credit rating agencies;
- Credit Default Swap spreads, financial agreements that compensate the buyer in the event of a default, which give an early warning of likely changes in credit ratings; and
- Sovereign ratings to select counterparties from only the most creditworthy countries.

6.10 The end product of this modelling system which indicate the relative creditworthiness of counterparties. The Council is satisfied that this service gives the required level of security for its investments. It is also a service which the Council would not be able to replicate using in-house resources.

The minimum credit rating criteria the Council use will be a Short-Term rating (Fitch or equivalents) of F1 and a long-term rating of A. In circumstances where ratings from all three agencies are not available, two acceptable ratings will be deemed as sufficient.

Where three ratings are published and all three do not meet our minimum criteria the counterparty will not be used until such a time as all three ratings meet the minimum criteria or the lowest rating is withdrawn.

6.11 The credit ratings will be monitored as follows:

- All credit ratings are reviewed weekly. The Council has access to Fitch, Moody's and Standard and Poor's credit ratings and is alerted to changes through its use of the Link Asset Services creditworthiness service. Ongoing monitoring of ratings also takes place in response to ad-hoc e-mail alerts from Link Asset Services.
- If a counterparty's or deposit scheme's rating is downgraded with the result that it no longer meets the Council's minimum criteria, the further use of that counterparty/deposit scheme as a new deposit will be withdrawn immediately.
- If a counterparty is upgraded so that it fulfils the Council's criteria, its inclusion will be considered for approval by the Strategic Director, Resources and Digital.

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

6.13 The Council has determined the minimum long term and short-term ratings it deems to be "high" for each category of investment. These "high" ratings allow investments of 365 days or less to be classified as **specified investments**. The Council's approved limits for this "high" credit rating for deposit takers is as follows:

High Rated	Fitch	Moody's	Standard &

			Poor's
Short Term (ability to repay short term debt)	F1	P1	A1
Long Term (ability to repay long term debt)	A	A2	A

6.14 In addition to the above specified investments, the Council has also fully considered the increased risk of **non-specified investments** and has set appropriate limits for non-high rated deposit takers. These are as follows:

Non- High Rated	Fitch	Moody's	Standard &Poor's
Short term	F1	P1	A1
Long term	A-	A3	A-

The selection of counterparties with an acceptable level of creditworthiness will be achieved by selecting institutions down to a minimum durational band within Link Asset Services weekly credit list of worldwide potential counterparties. The maximum maturity periods and amounts to be placed in different types of investment instruments are detailed in Appendix 6.

6.15 UK Government nationalised/part nationalised banks will have a maximum limit of 40% or £20m of total investment, all other counterparties will not exceed a maximum limit equal to 20% of total investments or £15m. Unless there are major changes in the level of investment balances throughout the year this limit will be reviewed prior to the commencement of each financial year.

6.16 Where more than one counterparty from a group is included on the counterparty list the group in total will be controlled by the above limits with the maximum limit being that of the parent company. Within the group each counterparty/subsidiary will have individual limits based on their creditworthiness although the total placed with the subsidiaries will not exceed the limit of the parent company. Subsidiaries that do not satisfy the minimum credit criteria will not be included.

6.17 A number of counterparties are also approved by the Strategic Director, Resources and Digital for direct dealing. These counterparties are included on the approved list and dealing will be within agreed limits. Direct dealing with individual counterparties must be approved by the Strategic Director, Resources and Digital prior to investments being placed.

UK Banks - Ring Fencing

6.18 The largest UK banks were required by UK law to separate core retail banking services from their investment and international banking activities by 1 January 2019. This is known as “ring-fencing”.

6.19 Ring-fencing is a regulatory initiative created in response to the global financial crisis which improves the resilience of banks by changing their structure. In general, simpler, lower risk activities will be offered by a ring-fenced Bank (RFB), whilst more complex and riskier activities will sit within a non-ring-fenced bank (NRFB).

Foreign Banks

6.20 The Council will continue to use UK banks irrespective of the UK sovereign rating, however non-UK banks domiciled in countries with a minimum sovereign rating of AA+ will be considered for inclusion on the approved list, they must also meet the high rated lending criteria and have operations based in the UK. Limits will be prescribed by the Link Asset Services creditworthiness list and limited to 365 days or less. Each country will be limited to the maximum investment limit of £15m or 20% of the Council's total investments. A list of those countries with a minimum sovereign rating of AA+ is shown in Appendix 7.

Local Authorities

6.21 The Council invests with other Local Authorities on an ad hoc basis; each investment is considered on an individual basis and agreed by the Strategic Director, Resources and Digital, prior to funds being placed. Limits are detailed at Appendix 6.

Investment balances / Liquidity of investments

6.22 Creditworthiness of counterparties is considered prior to depositing funds. The maximum term for investments is 3 years. Longer term deposits will continue where the counterparty is deemed to be a low credit risk to ensure a good rate of return is maintained in the current market conditions. Deposits beyond 365 days will only be considered when there is minimal risk involved. With deposits of this nature there is an increased risk in terms of liquidity and interest rate fluctuations. To mitigate these risks a limit of £15m (20% of total investments whichever is the higher) has been set and a prudential indicator has been calculated (See Appendix 4). Such sums will only be placed with counterparties who have the highest available credit rating or other local authorities.

6.23 Deposits for periods longer than 365 days are classed as **non-specified investments** and this will increase the total limit of overall deposits in this classification to 25%.

Non-Treasury Investments

6.24 The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure under the Local Government Act 2003. Such investments will have to be funded out of capital or revenue resources and will be classified as **'non-specified investments'**.

6.25 A loan or grant by the Council to another body for capital expenditure by that body is also deemed by regulation to be capital expenditure by the Council. It is therefore important for the Council to clearly identify if the loan was capital expenditure or if it is an investment made primarily to generate a financial yield. The latter will be assessed using the Council's Investment Framework.

6.26 The Council will ensure that all the organisation's investments are covered in either the Capital Strategy or Investment Strategy, and will set out, where relevant, the organisation's risk appetite and specific policies and arrangements for non-treasury investments. It will be recognised that the risk appetite for these activities may differ from that for treasury management.

6.27 To date the Council have not entered into any non-treasury investments which are purely to generate a commercial return, neither are there any plans to consider entering into non-treasury investments solely or primarily to obtain a revenue return. However, if an opportunity to do so arose the long term financial impact and the risks inherent to the scheme would be assessed as part of the due diligence process. Where the size of the investment or the risk of the investment required external advice, this will be obtained. Any potential investment entered for a commercial return will require prior Cabinet approval.

6.28 The Council does not invest for solely commercial reasons or to generate income to support the revenue budget. Any capital investment entered into to deliver service objectives and/or the placemaking role of the local authority is monitored and reported in line with the Capital Strategy. Capital investments are assessed in terms of their contribution to deliver the following objectives:

- Health and Housing
- Economy
- Poverty and Equality
- Climate Change
- Transport

Further information can be obtained from the Council's Capital Strategy at the following link: Capital Strategy 2020/21 to 2024/25

6.29 The Council maintains a schedule setting out a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and the organisation's risk exposure, which is attached at Appendix 8.

Internal Investment Strategy

6.30 The Strategic Director, Resources and Digital will monitor the interest rate market and react appropriately to any changing circumstances.

6.31 The Council takes the view that bank rate is forecast to increase steadily but slowly over the next few years to reach 1.00% by quarter 2 2021. Bank rate forecasts for financial year ends are 2019/20 0.75%, 2020/21 0.75% and 2021/22 1.00%.

6.32 The overall balance of risks to economic growth in the UK is probably relatively even due to the weight of all the uncertainties over post-Brexit trade arrangements and the impact of an expansionary government spending policy.

6.33 The balance of risks to increases or decreases in Bank Rate and shorter term PWLB rates are also broadly even.

Investment Risk Benchmark

6.34 The Council will use an investment benchmark to assess the investment performance of its investment portfolio against the 3-month London Interbank Bid Rate (LIBID). The Council is also a member of the Link Asset Services investment benchmarking Group who meet semi-annually. As a member, quarterly reports on comparative performance with other members of the group and the wider Link Asset Services client base are received. The benchmarking return for the group is a reasonable target for the Council, which allows the relative risk appetite to be considered as part of the benchmark.

End of year investment report

6.35 By the end of September each year Council will receive a report from Cabinet on its investment activity as part of its annual treasury report.

Policy on use of external service providers

6.36 The Council currently uses Link Asset Services as its external treasury management advisers.

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

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

Scheme of Delegation

6.39 As required by the Guidance Notes for Local Authorities the Treasury Management Scheme of Delegation is detailed in Appendix 3, paragraph 1.3.

Role of the Section 151 Officer

6.40 As required by the Guidance Notes for Local Authorities the role of the Section 151 Officer in relation to treasury management is detailed below:

- Recommending the Code of Practice to be applied, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;
- Submitting regular treasury management policy reports;
- Submitting budgets and budget variations;
- Receiving and reviewing management information reports;
- Reviewing the performance of the treasury management function;
- Ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;
- Ensuring the adequacy of internal audit, and liaising with external audit; and
- Arranging for the appointment of external service providers;
- Preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments and treasury management;
- Ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority;
- Ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing;
- Ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources;
- Ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities;

- Provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees;
- Ensuring that members are adequately informed and understand the risk exposures taken on by an authority;
- Ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above.

Appendix 4

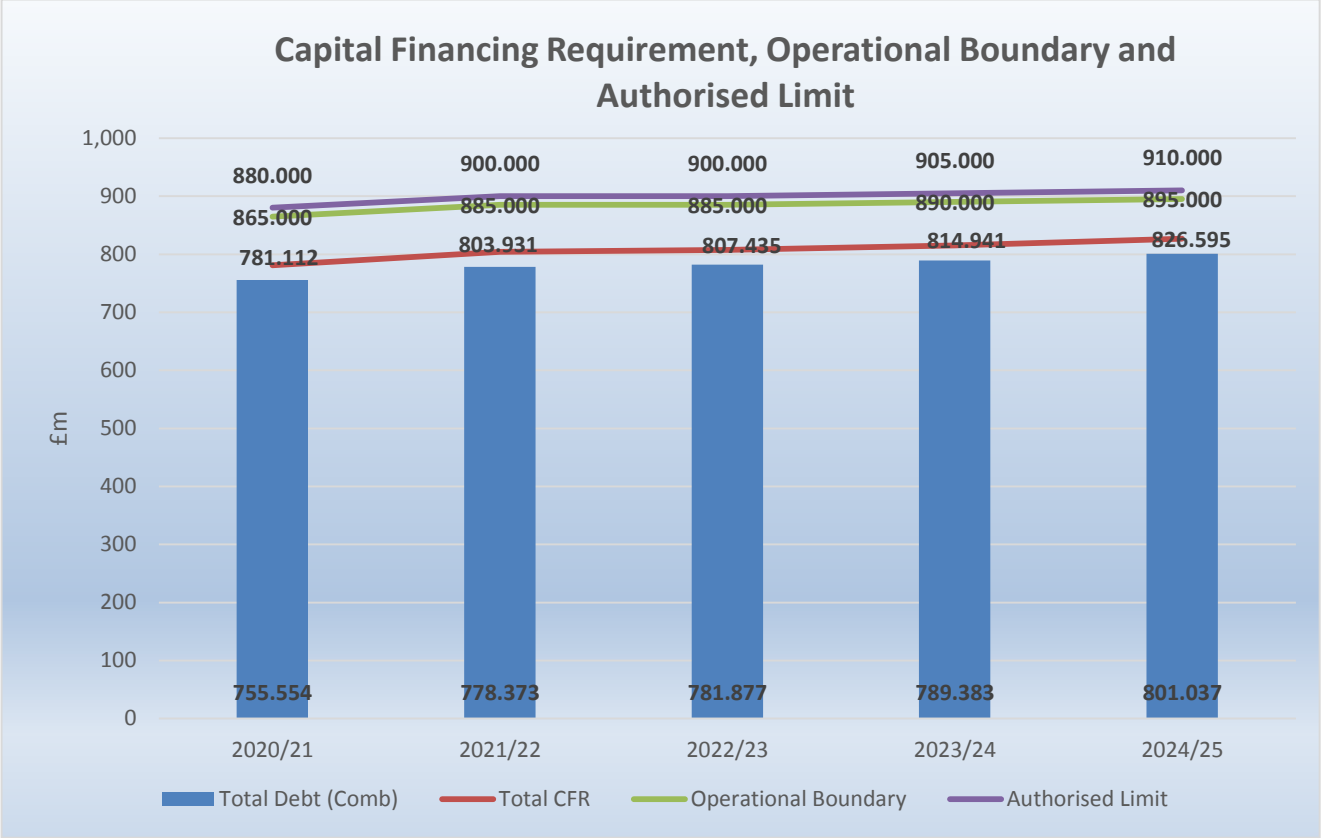
Prudential Indicators –Treasury Management

Authorised Limit for External Debt					
	2020/21 £000	**2021/22 £000**	**2022/23 £000**	**2023/24 £000**	**2024/25 £000**
Borrowing	880,000	900,000	900,000	905,000	910,000

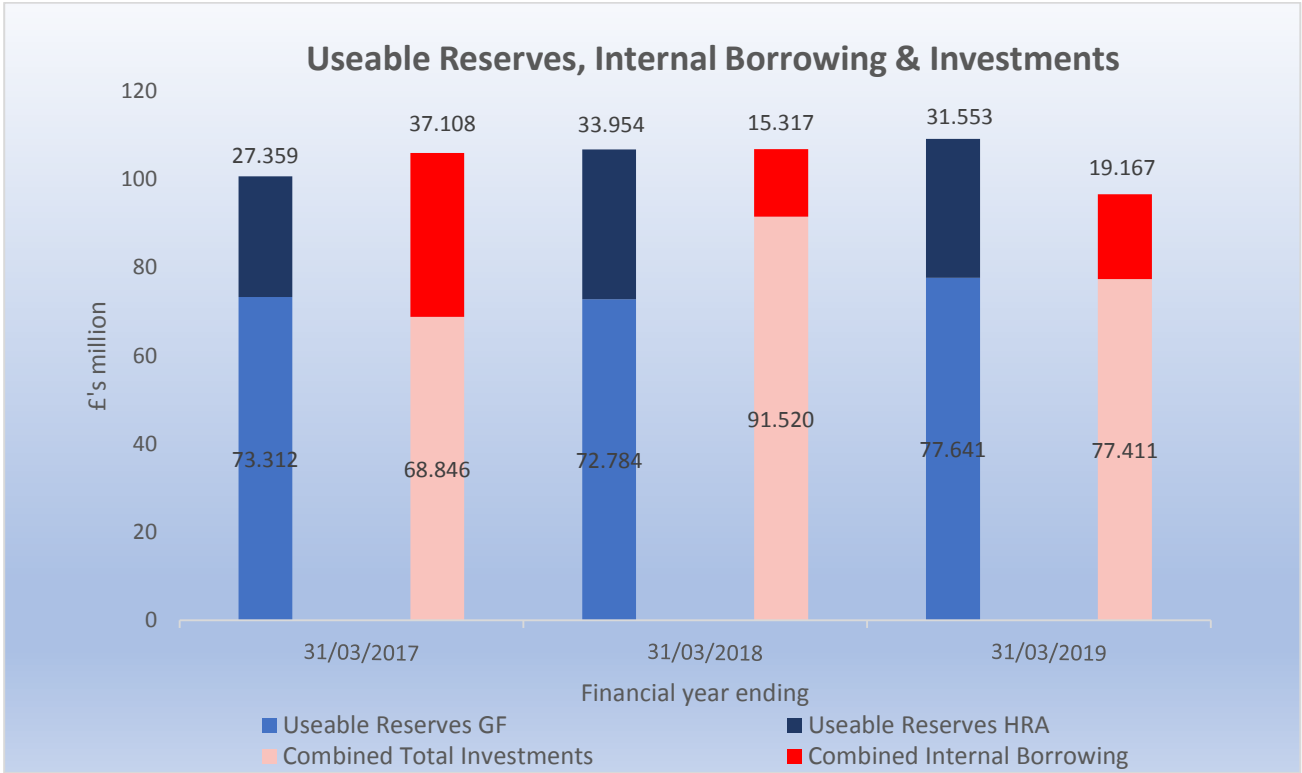
The Authorised Limit for External Debt sets the maximum level of external borrowing that the Council can incur. It reflects the level of borrowing which, while not desired, could be afforded in the short-term, but is not sustainable. It is the Council's expected maximum borrowing need with headroom for unexpected cashflow. The limit also provides scope for the Council to borrow in advance of need.

Operational Boundary for External Debt					
	2020/21 £000	**2021/22 £000**	**2022/23 £000**	**2023/24 £000**	**2024/25 £000**
Borrowing	865,000	885,000	885,000	890,000	895,000

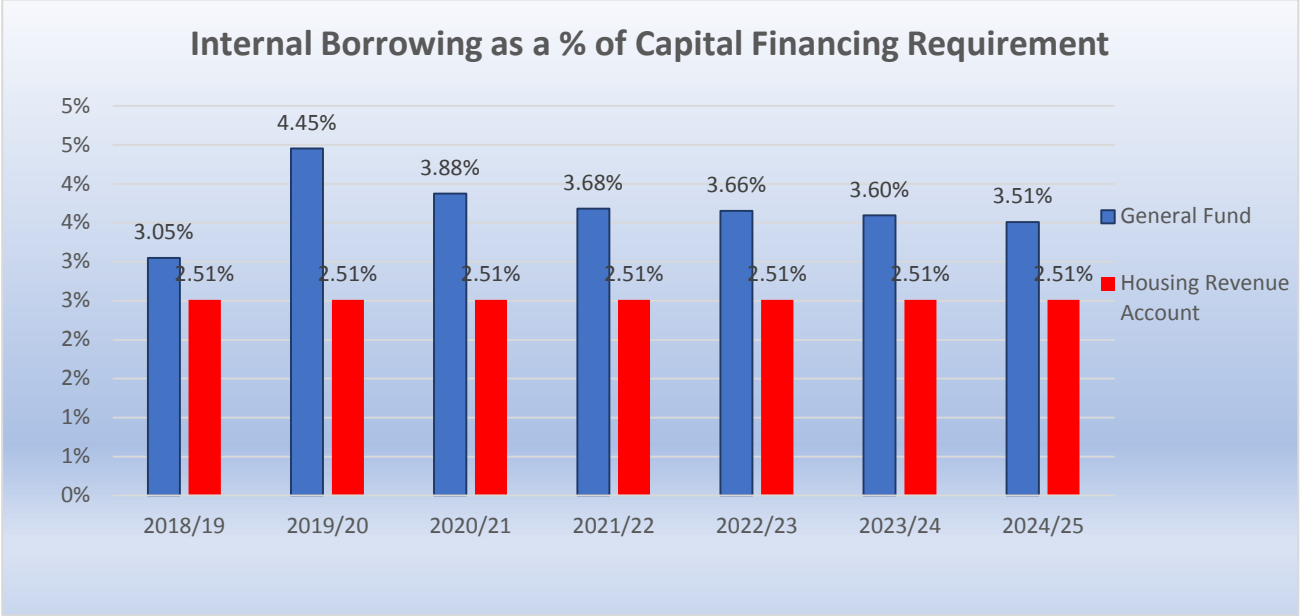
The Operational Boundary for External Debt is based on the probable external debt during the course of the year. It is not a limit and actual borrowing could vary around this boundary for short times during the year. It acts as an early warning indicator to ensure the authorised limit is not breached. Similar, to the authorised limit it also provides scope for the Council to borrow in advance of need.



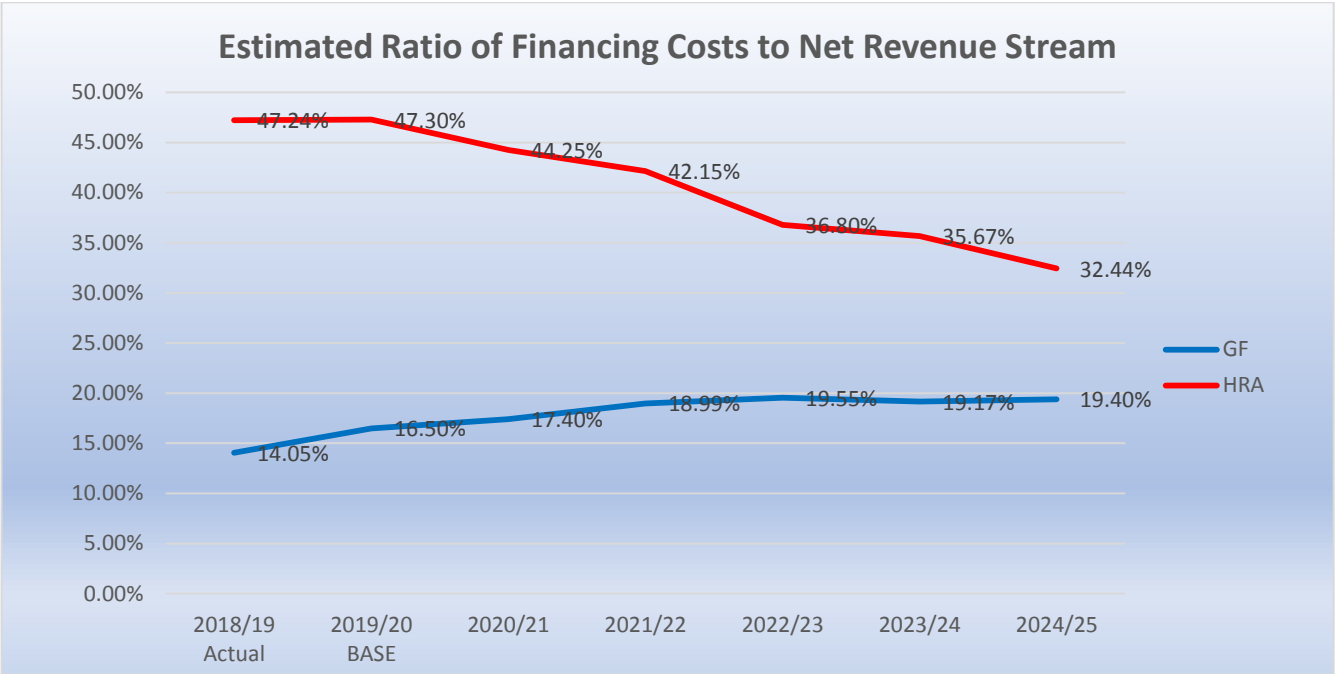
Capital Financing Requirement (CFR) shows the Council's capital borrowing requirement. Any gap between the CFR and the total debt highlights the potential to borrow further if the cashflow and treasury management position dictate.



The internal borrowing position represents the level to which reserves, and balances have temporarily been used to support borrowing positions and therefore the reserves will not be backed by cash in the bank.



Internal borrowing as a percentage of the Council's underlying borrowing requirement reflects the Council's exposure to interest rate movements and the element of borrowing that is being undertaken at variable rates (i.e. rates equivalent to the lost interest on investment income).



Ratio of financing costs to net revenue stream – financing costs must be met before any services have been delivered. Higher financing costs leaves less available to provide services.

Treasury Indicators

Upper and Lower Limits for the Maturity Structure of Fixed Rate Borrowings		
	Upper Limit	**Lower Limit**
Under 12 months	30%	0%
12 months and within 24 months	25%	0%
24 months and within 5 years	25%	0%
5 years and within 10 years	30%	0%
10 years and within 20 years	30%	0%
20 years and within 30 years	25%	0%
30 years and within 40 years	50%	0%
40 years and within 50 years	50%	0%
50 years and above	25%	0%

Upper and Lower Limits for the Maturity Structure of Variable Rate Borrowings		
	Upper Limit	**Lower Limit**
Under 12 months	25%	0%
12 months and within 24 months	20%	0%
24 months and within 5 years	20%	0%
5 years and within 10 years	20%	0%
10 years and within 20 years	20%	0%
20 years and within 30 years	20%	0%
30 years and within 40 years	20%	0%
40 years and within 50 years	20%	0%
50 years and above	20%	0%

Upper Limit on Amounts Invested Beyond 365 Days					
	2020/21 £000	**2021/22 £000**	**2022/23 £000**	**2023/24 £000**	**2024/25 £000**
Investments	15,000	15,000	15,000	15,000	15,000

Appendix 5

Specified Investments (All Sterling Denominated)

Investment type	**Share/ Loan Capital**	**Repayable/ Redeemable within 12 months**	**Security / Minimum Credit Rating**	**Capital Expend-iture**	**Circumstance of use**	**Maximum period**
Term deposits with the UK Government or with UK local authorities (i.e. local authorities as defined under Section 23 of the 2003 Act) with maturities up to 365 days.	No	Yes	High security although LA's not credit rated. *See appendix 3 Creditworthiness Policy*	No	In-house	365 days
Term deposits with credit-rated deposit takers (banks and building societies), including callable deposits with maturities up to 365 days.	No	Yes	Secure Varied minimum credit rating *See appendix 3 Creditworthiness Policy*	No	In-house	365 days

Short Term Money Market Funds The majority of these funds are instant access and therefore do not have a maturity date.	No	Yes	Secure Varied minimum credit rating *See appendix 3 Creditworthiness Policy*	No	In-house	The investment period is subject to liquidity and cash flow requirements. It is assumed that funds are placed overnight and will be returned and reinvested the next working day (although no actual movement of cash may take place).
Standard Money Market Funds and Ultra Short Duration Funds 3-day notice cash plus fund These funds require three-day notice for withdrawals and therefore do not have a maturity date.	No	Yes	Secure Varied minimum credit rating *See appendix 3 Creditworthiness Policy*	No	In-house	The investment period is subject to liquidity and cash flow requirements. Notice required is three days, however it is the intention to leave these funds for terms longer than other money market funds to achieve greater returns.

Non-Specified Investments (All Sterling Denominated)

Investment type	(A) Why use it (B) Associated risks	Share/ Loan Capital	Repayable/ Redeemable within 12 months	Security / Minimum credit rating	Capital Expenditure	Circumstance of use	Max % of overall investments	Maximum maturity of investment
Rated deposit takers (banks and building societies) which do not meet the Council's "high" credit rating	(A) To improve ability to place smaller amounts (B) Greater risk than "high" credit rating counterparties but advance warning by rating agency of potential problems. The Council has fully considered this investment category and set appropriate investment and maturity limits in order to minimise risk.	No	Yes	Secure Varied minimum Credit rating *Minimum: Long term A-* *Short term F1*	No	In-house	Total not high rated deposits as a proportion of total investments 25%	6 months (but set on an individual counterparty basis)
Term deposits with UK Government, UK Local Authorities or credit rated banks and building societies, with maturities over 1 year	A) To improve the ability to "lock in" at times of high interest rates to secure a higher return over a longer period should rates be forecast to fall. B) Lower liquidity and greater risk of adverse interest rate fluctuations. The Council has fully considered this investment category and set appropriate investment and maturity limits in order to minimise risk.	No	No	Secure Varied minimum credit rating	No	In-house	Total investment per Counterparty 20%	3 years

Certificate of Deposits issued by banks and building Societies	A) Provides additional counterparties, as many banks do not want to take fixed term cash deposits. B) Credit risk could change but if adverse there is an option to sell onto a secondary market. The Council has fully considered this investment category and set appropriate investment and maturity limits in order to minimise risk.	No	Yes	Secure Varied minimum Credit rating *Minimum: Fitch Long term A- Short term F1*	No	In-House	20%	12 months (but set on an individual counterparty basis)

Appendix 6

Maximum Maturity Periods and Amounts

Organisation	**Criteria**	**Max Amount***	**Max Period**
High Rated (Specified Investments – High rated and up to 365 days see Appendix 5) Foreign Banks	Minimum Fitch rating of F1 short term and A long term. Moody's minimum rating of P1 short term backed by A2 long term and S&P minimum rating of A1 short term and A long term. Must meet the minimum high rated criteria above and have a minimum sovereign rating of AA+	£20m (Gov't Backed, otherwise £15m) £15m country limit	3 years 365 Days
Non-High Rated	Minimum Fitch rating of F1 short term and A- long term. Moody's minimum rating of P1 short term backed by A3 long term and S&P minimum rating of A1 short term and A- long term.	£10m	6 months
UK Local Authorities	(i.e. local authorities as defined under Section 23 of the 2003 Act) Each investment is considered on an individual basis	£10m	3 years
Short-Term Money Market Funds (Same day settlement)	AAA mmf fund rating or equivalent with assets >£1bn	£10m	Overnight
Standard Money Market Funds and Ultra-Short Duration Funds (Trade plus 3-day settlement)	AAAf fund rating or equivalent, backed up with lowest volatility rating (S1) or equivalent with assets > £0.75bn	£10m	3 days

* Restricted to a maximum of either 40% if government backed or 20% of total investments if non-government backed counterparty.

Foreign Banks **Appendix 7**

This list is based on those countries which have non-UK sovereign ratings of AA+ or higher at 03/01/20.

AAA

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

AA+

- Finland
- U.S.A.

Non-Treasury Management Investments **Appendix 8**

Investment	Latest Balance	Notes
Long term loans to Keelman Homes	13,041,102.00	Loan balance at 31/1/20
SCAPE System Build Ltd.	784,000.00	17% Shareholding in SCAPE
Newcastle International Airport	11,693,076.00	13.33% shareholding in Newcastle Airport
Hospital of King James	67,274.39	Loan balance at 31/1/20
Loan to Citizens Advice Bureau	515,622.90	Loan balance at 31/1/20
Loan to Trading Company	6,369,000.00	Loan balance at 31/1/20
Newcastle International Airport Long Term Loan Notes	10,289,654.00	Loan Notes - interest paid bi annually - principal repayment due 2032
Soft Loans	351,290.65	North Music Trust - Soft Loan

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