

Notice of meeting of

Audit & Governance Committee

To:	Councillors Jeffries (Chair), Barnes, Brooks (Vice-Chair), Burton, Cuthbertson, Watson and Steward
Date:	Monday, 5 December 2011
Time:	5.30 pm
Venue:	The Guildhall, York

AGENDA

1. **Declarations of Interest**

At this point Members are asked to declare any personal or prejudicial interests they may have in the business on this agenda.

2. **Minutes** (Pages 3 - 10)

To approve and sign the minutes of the meeting held on **29 September 2011**.

3. **Public Participation**

It is at this point in the meeting that members of the public who have registered their wish to speak regarding an item on the agenda or an issue within the Committees remit can do so. The deadline for registering is **5:00pm on Friday 2nd December 2011**.

4. **Forward Plan.** (Pages 11 - 16)

This paper presents the future plan of reports expected to be presented to the Committee during the forthcoming year to September 2012.

5. Key Corporate Risk Monitor Quarter 3. (Pages 17 - 34)

The purpose of this paper is to present to Audit & Governance Committee (A&G) an overview of the risks associated with the councils Key Corporate Risks (KCRs) as at November 2011.

6. Annual Audit Letter. (Pages 35 - 54)

This paper introduces the Annual Audit Letter 2010/11 (see annex A) prepared by the Audit Commission together with the Council's response.

7. Review of the Effectiveness of Internal Audit 2011/12. (Pages 55 - 58)

This reports asks Members to agree the arrangements for the 2011/12 review of the effectiveness of internal audit.

8. Internal Audit and Fraud Plan Progress Report. (Pages 59 - 78)

This report provides an update on progress made in delivering the internal audit work plan for 2011/12 and on current counter fraud and information governance activity. The report also includes details of a proposed expansion of Veritau.

9. Scrutiny of the Treasury Management Monitor 2 Report 2011/12 and Review of Prudential Indicators. (Pages 79 - 100)

This report reviews the economic market conditions in which the treasury management activities of the council are currently operating. Appendix A provides Members with an update of treasury management activity for the first six months of 2011/12.

10. Urgent Business

Any other business which the Chair considers urgent under the Local Government Act 1972

Democracy Officer:

Name – Laura Bootland

Telephone No. – 01904 552062

E-mail – laura.bootland@york.gov.uk

For more information about any of the following please contact the Democracy Officer responsible for servicing this meeting:

- Registering to speak
- Business of the meeting
- Any special arrangements
- Copies of reports

Contact details are set out above.

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Further information about what's being discussed at this meeting

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Holding the Executive to Account

The majority of councillors are not appointed to the Executive (40 out of 47). Any 3 non-Executive councillors can 'call-in' an item of business from a published Executive (or Executive Member Decision Session) agenda. The Executive will still discuss the 'called in' business on the published date and will set out its views for consideration by a specially convened Scrutiny Management Committee (SMC). That SMC meeting will then make its recommendations to the next scheduled Executive meeting in the following week, where a final decision on the 'called-in' business will be made.

Scrutiny Committees

The purpose of all scrutiny and ad-hoc scrutiny committees appointed by the Council is to:

- Monitor the performance and effectiveness of services;
- Review existing policies and assist in the development of new ones, as necessary; and
- Monitor best value continuous service improvement plans

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- Councillors get copies of all agenda and reports for the committees to which they are appointed by the Council;
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City of York Council

Committee Minutes

MEETING	AUDIT & GOVERNANCE COMMITTEE
DATE	29 SEPTEMBER 2011
PRESENT	COUNCILLORS JEFFRIES (CHAIR), BARNES, BROOKS (VICE-CHAIR), BURTON, CUTHBERTSON, WATSON AND STEWARD CRISP (IN ATTENDANCE)

21. DECLARATIONS OF INTEREST

At this point in the meeting, Members were asked to declare any personal or prejudicial interests they may have in the business on the agenda.

Councillor Brooks declared a personal non prejudicial interest as a member of the Teachers Pension Scheme.

Councillor Barnes declared a personal non prejudicial interest as a trustee of York Museums Trust.

22. MINUTES

RESOLVED: That the minutes of the Audit and Governance meeting held on 26 July 2011 be approved and signed by the Chair.

23. PUBLIC PARTICIPATION

It was reported that there had been no registrations to speak under the Council's Public Participation Scheme.

24. FORWARD PLAN.

Members considered a report which presented the future plan of reports expected to be presented to the Committee during the forthcoming year to July 2012.

Officers reported that there had been no amendments to the Forward Plan since the previous version had been presented to the Committee in July 2011.

Members queried if any training sessions had been planned for the Committee. Officers confirmed that they are intending to hold a training session in November and requested that Democratic Services look into Members availability.

RESOLVED: (i) That the Committee's Forward Plan for the period up to July 2012 be noted.

(ii) That Members identified no further items for the forward plan.

REASON: To ensure the Committee receives regular reports in accordance with the functions of an effective audit committee.

25. FINAL STATEMENT OF ACCOUNTS 2010/11.

Members considered a report which brought to their attention the revised and final set of Accounts for 2010/11. The accounts reflected changes that had been made since the draft pre-audit accounts were presented to the Audit and Governance Committee for review in line with CIPFA best practice.

The Statement of Accounts were attached at Annex A and Officers advised that the 4 core statements had been adjusted which resulted in the notes attached to the accounts also being adjusted. Members noted that the changes had no effect on the budget outturn position of the Council.

RESOLVED: That Members noted the Final Statement of Accounts for 2010/11 in order that they can receive the Annual Governance Report of the Audit Commission that was agenda item 6 on the agenda.

REASON: It is a statutory requirement that a committee of the Council or Full Council approves the Statement of Accounts for 2010/11 by 30th September 2011.

26. ANNUAL GOVERNANCE REPORT 2010/11.

Members considered a report that brought to their attention the Audit Commission's Annual Governance Report (Annex A to the report). Representatives from the Audit Commission went through the key issues.

Members were asked to agree the letter of representation and to approve changes to the 2010/11 Financial Statements.

The Auditors drew Members attention to the following three issues regarding the quality of the financial statements:

- The statements contained errors, although Officers had identified a number of amendments themselves.
- The implementation of International Financial Reporting Standards (IFRS) and Code requirements had caused increased pressure for Officers.
- Meeting the submission deadline for the Whole Government Accounts work had been challenging.

Members referred to page 12 of the Governance Report and to the fact that the central partnership team had recently been wound up and raised concerns about how the Council would continue ensure that it is receiving value for money from partnerships. Members requested further information on the outcome and achievements of partnerships.

RESOLVED: (i) That the Annual Governance Report be noted.

(ii) That in respect of the items identified as material misstatements on pages 5 and 6 of the Annual Governance Report at Annex A (Errors in financial statements) the Statement of Accounts 2010/11 be amended for those items.

(iii) That in respect of the items identified on page 6 of the Annual Governance Report, at Annex A, (Errors and uncertainties not adjusted), the Statement of Accounts not be amended for those items.

- (iv) That subject to the agreed amendments, the Statement of Accounts 2010/11 be approved.
- (v) That the letter of representation be approved and signed by the Chair.
- (vi) That the anticipated receipt of an unqualified Audit Opinion to both the Statement of Accounts 2010/11 and the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources be noted.
- (vii) Officers to provide Members with further information on the outcomes of partnerships.¹

- REASONS:
- (i) To ensure the proper consideration of the opinion and conclusions of the External Auditor in respect of the annual audit of accounts and review of the Council's arrangements for ensuring value for money.
 - (ii) To ensure compliance with International Auditing Standards and relevant legislative requirements.
 - (iii) To ensure Members of the Audit and Governance Committee are aware of any matters arising from the annual audit of the Statement of Accounts.

Action Required

1. Provide Members with requested information.

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27. ANNUAL REPORT OF THE AUDIT AND GOVERNANCE COMMITTEE.

Members considered a report which sought their views on the draft annual report of the Audit and Governance Committee for the year ending 30 September 2011, prior to its submission to Full Council. The report also presented a draft assurance statement which the Committee has been requested to provide to the Council's external auditors, the Audit Commission.

Members commented that they were happy with the contents of the report.

- RESOLVED: (i) That Members considered the report and commented as above.
- (ii) That Members approved the wording of the assurance statement to the external auditor from 'those charged with governance' and confirm the statement can be signed on behalf of the Audit and Governance Committee by the Chair.

REASON: To enable the Committee to fulfil its role in providing assurance about the adequacy of the Council's internal control environment and arrangements for managing risk and for reporting on financial and other performance.

28. KEY CORPORATE RISK MONITOR 2.

Members considered a report which presented to them an overview of the risks associated with the Councils Key Corporate Risks (KCR's) as at the end of August 2011.

Officers were asked why some corporate risks, such as the Fairness and Inclusion risk appear very broad where as others are more specific. They explained that some risks are more wide ranging and are continuously monitored and in order to be improved upon.

- RESOLVED: (i) That Members considered and noted the key corporate risks set out at paragraphs 5 and 6 respectively.
- (ii) That Members considered the directorate risks for CBSS and OCE set out at Annex A and B respectively.

- REASONS: (i) To provide assurance that risks to the council are continuously reviewed and updated.
- (ii) To provide assurance that risks to the Council are continuously reviewed and managed at directorate level.

29. FOLLOW UP OF INTERNAL AND EXTERNAL AUDIT RECOMMENDATIONS.

Members considered a report which gave the regular six monthly update to the Committee. The report set out progress made by Council departments in implementing agreed actions as part of internal audit work.

Officers responded to Members queries in respect of actions outlined in paragraph 9 that had no suitable action taken.

Officers agreed to provide more information in future reports regarding future trends on implementing agreed actions as a result of audit work.

RESOLVED: That Members of the Audit and Governance Committee were asked to:

- (i) Consider the progress made in implementing internal audit agreed actions as reported in paragraphs 5 to 10.
- (ii) Note that changes will be made in the escalation procedure in agreement with the Assistant Director, Financial Services.

REASON: To enable Members to fulfil their role in providing independent assurance on the councils control environment.

30. AUDIT, COUNTER FRAUD AND INFORMATION GOVERNANCE MONITORING REPORT.

Members considered a report that set out the progress made in delivering the internal audit work plan for 2011/12 and on current counter fraud and information governance activity.

RESOLVED: (i) That Members noted the progress made in delivering the 2011/12 internal audit work programme and current counter fraud and information governance activity.

(ii) That Members noted the variations to the 2011/12 audit plan as set out in annex 2 to the report.

REASON: (i) To enable Members to consider the implications of audit and fraud findings.

(ii) To enable Members to consider the delivery of the internal audit plan.

Councillor Jeffries, Chair

[The meeting started at 2.00 pm and finished at 3.30 pm].

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Audit and Governance Committee

5 December 2011

Report of the Assistant Director of CBSS (Financial Services)

Audit & Governance Committee Forward Plan to September 2012**Summary**

1. This paper presents the future plan of reports expected to be presented to the Committee during the forthcoming year to September 2012.

Background

2. There are to be six fixed meetings of the Committee in a municipal year. To assist members in their work, attached as an Annex is the indicative rolling Forward Plan for meetings to September 2012. This may be subject to change depending on key internal control and governance developments at the time. A rolling Forward Plan of the Committee will be reported at every meeting reflecting any known changes.
3. Several amendments to the forward plan have been made since the previous version was presented to this Committee in September 2011. These reflect the planned work of the Council's External Auditors over the next 12 months.

Consultation

4. The Forward Plan is subject to discussion by members at each meeting, has been discussed with the Chair of the Committee and key corporate officers.

Options

5. Not relevant for the purpose of the report.

Analysis

6. Not relevant for the purpose of the report.

Corporate Priorities

7. This report contributes to the overall effectiveness of the council's governance and assurance arrangements contributing to an 'Effective Organisation'.

Implications

- 8.
- (a) **Financial** - There are no implications
 - (b) **Human Resources (HR)** - There are no implications
 - (c) **Equalities** - There are no implications
 - (d) **Legal** - There are no implications
 - (e) **Crime and Disorder** - There are no implications
 - (f) **Information Technology (IT)** - There are no implications
 - (g) **Property** - There are no implications

Risk Management

9. By not complying with the requirements of this report, the council will fail to have in place adequate scrutiny of its internal control environment and governance arrangements, and it will also fail to properly comply with legislative and best practice requirements.

Recommendations

- 10.
- (a) The Committee's Forward Plan for the period up to September 2012 be noted.

Reason

To ensure the Committee receives regular reports in accordance with the functions of an effective audit committee.

- (b) Members identify any further items they wish to add to the Forward Plan.

Reason

To ensure the Committee can seek assurances on any aspect of the council's internal control environment in accordance with its roles and responsibilities.

Contact Details

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Chief Officer Responsible for the report:

Keith Best
Assistant Director of CBSS (Financial
Services)
Telephone: 01904 551745

**Report
Approved**



Date 14/11/2011

Specialist Implications Officers

Head of Civic, Democratic & Legal Services

Wards Affected: Not applicable

All

For further information please contact the author of the report

Background Papers:

None

Annex

Audit & Governance Committee Forward Plan to September 2012

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Audit & Governance Committee Draft Forward Plan to September 2012

Training/briefing events will be held at appropriate points in the year to support members in their role on the Committee.

- **Committee 13 February 2012**

Key Corporate Risk Monitor Quarter 4 (including ACE risks)

Scrutiny of the Treasury Management Monitor 3 Report 2011/12 and Review of Prudential Indicators

Scrutiny of the Treasury Management Strategy Statement and Prudential Indicators for 2012/13 to 2016/17

Update of Counter Fraud Policies

Internal Audit Plan Consultation

Audit & Fraud Risk Assessment

*Audit Commission reports as per agreed Audit & Inspection plan
Changes to the Constitution (if any)*

- **Committee 2 April 2012**

Approval of Internal Audit Plan

Internal Audit & Fraud Plan Progress Report

Follow up of Internal and External Audit Recommendations

Review of the Effectiveness of the Audit & Governance Committee

Audit Commission national reports summary (if any)

*Audit Commission reports as per agreed Audit & Inspection plan
Changes to the Constitution (if any)*

- **Committee June 2012 (Date TBC)**

Review of the Effectiveness of Internal Audit

Annual Report of the Head of Internal Audit

Draft Annual Governance Statement 2011/12

*Audit Commission reports as per agreed Audit & Inspection plan
Changes to the Constitution (if any)*

- **Committee July 2012 (Date TBC)**

External Audit 2011/12 Audit Progress report

Draft Statement of Accounts 2011/12

Scrutiny of the Treasury Management Annual Report 2011/12 and
Review of Prudential Indicators

Key Corporate Risk Monitor Quarter 1

*Audit Commission national reports summary (if any)
Audit Commission reports as per agreed Audit & Inspection plan
Changes to the Constitution (if any)*

- **Committee September 2012 (Date TBC)**

2011/12 Final Statement of Accounts

Annual Governance Report 2011/12

Annual Report of the Audit & Governance Committee

Key Corporate Risk Monitor Quarter 2 including CBSS and OCE
Risks

Follow-up of Internal and External Audit Recommendations

Internal Audit & Fraud Plan Progress Report

*Audit Commission reports as per agreed Audit & Inspection plan
Changes to the Constitution (if any)*



Audit & Governance Committee

5 December 2011

Report of the Assistant Director CBSS (Financial Services)

Key Corporate Risk Monitor Three 2011/12

Summary

1. The purpose of this paper is to present to Audit & Governance Committee (A&G) an overview of the risks associated with the council's Key Corporate Risks (KCRs) as at November 2011.

Background

2. The High and Critical KCRs are reported to A&G four times a year and at least twice a year to Corporate Management Team (CMT) as part of the council's overall governance arrangements. The KCRs along with directorate level risks are also regularly reviewed at Directorate Management Teams (DMT's).

Changes to the way risk are reported

3. As approved at A&G on the 26 July 2011 as well as providing an overview of High and Critically ranked KCRs each quarter the monitor now also provides directorates the opportunity to present an overview of their own High and Critical risks. This is being delivered on a rolling programme. CBSS & OCE delivered their risk reports at the last A&G committee in September 2011. The rest of the directorates will present their risks to A&G during the course of the year. The full year programme for 2011/12 is set out at Table 1 below.

Table 1

<u>A&G Committee</u>	<u>Directorate</u>
<u>Date</u>	
29 September 2011	- Customer & Business Support Services/Office of the Chief Executive
5 December 2011	- Community & Neighbourhoods/City Strategy
13 February 2012	- Adults Children & Education

4. The two Directorates presenting their risk registers at monitor three are City Strategy (CS) and Communities and Neighbourhoods (CAN's). Their overviews are set out at Annex A and B respectively.

Monitor 3

5. There has been no change in the number of critical KCRs since Monitor 2 2011/12. There are three critical risks corporately and the up to date risk owners comments are set out below:

KCR 0016 Capital Programme

Failure to obtain funding for Access York Phase 1

'The delivery risk for Access York Phase 1 is considered to be critical because the way that the government distributes funding for transport major schemes has significantly altered since the scheme obtained Programme Entry status in March 2010. The other key risks such as planning consent and land purchase have all been resolved satisfactorily but the availability of the principal funding source, confirmed by the previous administration, is now more uncertain.

To maximize the likelihood of funding being provided the project put forward to the DfT has been reduced in scope to the Askham Bar and Poppleton Bar sites and associated works only. In addition the funding allocation from the Council has been increased to £6.6m representing

approximately 30% of the total £21.9m cost. A Best and Final Funding Bid for these two sites was submitted to the DfT on 9 September. 45 schemes valued at approx. £870m are bidding for £600m of funds. A decision is expected in December 2011. Alternative funding sources for the remaining site at Clifton Moor are being investigated.

If the Access York Phase 1 scheme is successful in obtaining funding, it is anticipated that the project would be completed and the Park & Ride sites operational, by summer 2014.'

KCR 0019 Safeguarding

Safeguarding

"In common with every other local authority this risk remains a constant. The controls in place are regularly reviewed and updated in line with emerging national guidance. Measures to review and strengthen the controls in place to manage this risk in the next quarter include, participation in an LGID Peer Review of our Local Safeguarding arrangements, implementation of our local action plan following the recent unannounced inspection of our contact, referral and assessment service, implementation of a new supervision policy for all children's social care workers involved in child protection activity and improved case file auditing arrangements."

KCR 0022 Financial Pressures

Reduction in Revenue Budgets

"The requirement to reduce revenue budgets by approximately 28% and a 45% reduction in capital funding over the next 4 years presents a challenging financial scenario for the council to manage. Whilst long term financial planning provides a key control, critical to the organisation being able to manage this risk effectively lies in identifying and achieving the savings identified in service reviews and delivered through the Business Change & Performance (BCP) efficiency program."

6. There remains 14 High key corporate risks as reported to A&G in September 2011:

Ageing Population – KCR 0018

- Increasing social care support costs (Graham Terry);
- Understanding & responding to the demands of an ageing population (Graham Terry).

Fairness & Inclusion – KCR 0015

- Vulnerable people are unable to access our services including employment opportunities (Pauline Stuchfield);
- Councillor's vision and expectations of a fair inclusive and customer-focussed organisation will not be realised (Sally Burns);
- We do not provide fair and inclusive customer-focused services (Sally Burns);
- Vulnerable staff are bullied, harassed and feel excluded (Sally Burns).

Financial Pressures – KCR 0022

- Savings identified beyond 2011/12 are not achieved (Keith Best);
- Reduced levels of economic development due to less investment in national & regional transport infrastructure (Richard Wood).

Waste Management Strategy – KCR 0003

- Delays to the project (Bill Woolley);
- Failure to secure planning consent on any of the selected sites (Bill Woolley).

Emergency Planning – KCR 0010

- Inability to respond to and assist in the recovery of city of York following a major incident (Richard Wood);
- Inability to continue to deliver services following a business disruption event (Richard Wood).

Capital Programme – KCR 0016

- Administration & Accommodation Review – Developers unable to meet the requirements of the development brief (Ian Asher);
- Administration & Accommodation Review – Failure to discharge planning conditions (Ian Asher).

7. The appropriate risk owner from the relevant directorate can provide more detailed information, if it is required, in relation to any of the above risks.

Directorate Risks

8. The risks in respect of CS and CAN's are attached to this report at Annex A and B respectively. Officers from both directorates are in attendance to answer any queries you have in respect of the risks contained within these annexes.

Directorate High & Critical Risks

9. In terms of high and critical directorate risks there are none requiring escalation to A&G for this monitor.

Options

10. Not applicable.

Corporate Strategy

11. The effective consideration and management of risk within all of the council's business processes will contribute to achieving and delivering the council plan and support the successful delivery of each of the five priorities.

Implications

- (a) **Financial** - There are no implications

(b) **Human Resources (HR)** - There are no implications

(c) **Equalities** - There are no implications

(d) **Legal** - There are no implications

(e) **Crime and Disorder** - There are no implications

(f) **Information Technology (IT)** - There are no implications

(g) **Property** - There are no implications

Risk Management

12. In compliance with the council's Risk Management Strategy, there are no risks directly associated with the recommendations of this report. The activity resulting from this report will contribute to improving the council's internal control environment.

Recommendations

13. A&G are asked to:

a. Consider the key corporate risks set out at paragraph 5 and 6 respectively;

Reason

To provide assurance that risks to the council are continuously reviewed and updated

b. Consider the directorate risks for CS & CAN's set out at Annex A and B respectively;

Reason

To provide assurance that risks to the council are continuously reviewed and managed at directorate level.

Contact Details

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Phone No. 01904 552261

Chief Officer Responsible for the report:

Keith Best
Assistant Director of Financial Services
Customer and Business Support
Services

**Report
Approved**

Date

Specialist Implications Officer(s) Not applicable

Wards Affected Not applicable

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For further information please contact the author of the report

Background Papers

Key Corporate Risk Monitor Two 2011/12.

Annexes

- Annex A – CS Risks
- Annex B –CAN’s Risks

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Council Priority	Council outcome	Risk	Impact	Mitigations
Core Capabilities	A relentless focus on our priorities	Reduced funding	Job loses and cuts in services this will impact on customer satisfaction and staff morale. Levels of sickness may increase due to staff stress.	All managers are involved in reviewing services to cut out waste or increase income. Staff are updated with regards the current financial climate and asked to contribute ideas for remodelling services . Staff sickness is regularly reported and monitored. The Corporate Health and Wellbeing initiatives are available to staff
Core Capabilities	A relentless focus on our priorities	Inability to meet income targets	The directorate's budget is reliant on large values of income from car parking and planning. Budget overspend putting pressure on other priority areas.	Effective and consistent financial reporting by key budget variables. DM management through remediation plan if necessary

Core Capabilities	Capital Programme Review	Failure to manage and deliver a significant Capital Programme	Failure to deliver on these externally funded schemes will restrict the Councils ability to secure future capital funds for vital infrastructure works and improvements to its assets. Failure to deliver will hinder the council's ability to provide improved services to its customers. Failure to do this in turn will have a	Undertake effective project management. . Commission contract using the contract framework
Core Capabilities	A relentless focus on our priorities	At risk of adverse possession which means the title to another's property can be acquired without compensation. In the council's case, it does not hold deeds for some of its assets.	This can mean the permanent loss of the council's interest in the property and as a result a reduction in capital receipts.	Statutory regulation, statement of truth, retrospective registration.
Core Capabilities	Health and well-being	Possible accidental asbestos exposure	Potential exposure of personnel to airborne asbestos fibres and resultant risk of developing a harmful medical condition i). Potential for criminal proceedings by HSE against CYC iii). Potential for civil	Asbestos policy and training, annual audits of premises, liaison officers at each site. Type 3 surveys carried out before commencement of any refurbishment work.

Core Capabilities	Health and well-being	Potential for people to contract Legionnaire's Disease	Risk of personnel developing Legionnaire's disease from contaminated water in CYC premises ii). Risk of personnel being scalded by using hot water outlets in CYC premises iii). Risk of Criminal proceedings implemented by HSE iv). Risk of Civil	All sites - installations have been assessed for water risks Water risks monitoring regime in place on all CYC sites System in place to address any high risk situations Site Legionella Representatives appointed for all sites Periodic training sessions available for relevant staff Maintenance regime for water storage systems and shower
Core Capabilities	Health and well-being	Hot water outlet scalding	Member of staff or the public significantly scolded	Hot water blenders are installed in appropriate properties to control tap water temperature Individual management of shower water temperature Include water temperature management for scalding in policy document
Core Capabilities	Health and well-being	Failure to comply with Regulatory Reform (Fire Safety) Order 2005	Potential for fatality or injury of personnel working in, occupying or visiting CYC premises Potential for criminal proceedings being implemented by HSE Potential for civil proceedings	Fire Safety Risk Assessments and inspections, Fire wardens, periodic fire drills. Fire safety to be included in all regular premises H&S inspections Log of all fire drills and inspections to be maintained on site

Build Strong Communities	Safer Inclusive Communities	Failure to adhere to the requirements of the Single Equalities Act and implement the requirements of the act within prescribed timescales	The Council could be in breach of the requirements of legislation and inspection bodies. This can result in legal action, fines and poor inspection results. Failure to move from Achieving to Excellent for the Equalities Framework	Developing action plan to address the findings of the peer inspection and strengthen areas to move from achieving to excellent. Corporate commitment from ELG to DEL to Departmental Equality Networks. Equality Impact Assessment embedded in service and policy changes. Regular reporting on equality progress and issues
Get York Moving	Improving movement in the city centre	Highway Management Breach of Statutory Duty	Resources not available and/or systems not working. In relation to the Traffic Management Act failure to manage the Highway network to the maximum efficiency could result in the	Adequate numbers of suitably qualified and well trained staff. Financially supported technology. Ring fencing of Budgets. Executive recognition of the affect of policy decisions upon the Statutory obligations of the Traffic Management
Get York Moving	Winning hearts and minds	- Failure to deliver Intelligent Travel York Project	Failure to deliver relevant schemes on the ground to qualify for the relevant funding	Reporting and submission of claims to DfT on a quarterly basis. Intelligent Travel York schemes prioritised for delivery within Capital Programme

Core Capabilities	Improve our procurement	Potential challenge by European Commission or third party over procurement contracts	If the service does not follow the council's internal and also European regulations. This could lead to a failure to obtain the best balance of quality and cost in the procurement process.	Checks to ensure consistency of information supplied in documentation Contract awards to be signed by an officer with the appropriate delegated authority Review of tendering procedures OJEU notice issued in time to comply with regulations
Jobs and Economy	Positioning York on the Global Stage	Impact of international events	International event impact on visitor numbers requiring monitoring and effective service delivery response.	Constant monitoring
Core Capabilities	A confident and collaborative organisation	Delays to moving into West Offices	Completion of the construction work and the subsequent handover of the building to the council could be delayed. The council may not be entitled to occupy and/or use the building if planning conditions are not discharged.	Planning policy and the conditions attached to the planning approval Conditional Sale and Development Agreement. Staged design development meetings. Monitor discharge of CSDA pre-conditions including developer's discharging of the planning conditions.

Core Capabilities	A confident and collaborative organisation	Potential increase to an average 5:3 staff to desk ratio within West Offices	Services potentially unable to operate effectively at 5:3 staff to desk ratio. Additional cost of ICT solutions. Staff motivation affected. Potential increase in rentable space, Possible requirement for a desk booking system	Business needs analysis, design brief , change control process, service realignment plans
Jobs and Economy	Unlocking infrastructure to support investment	York North West does not proceed	Failure to meet housing and economic targets Community benefit for city not achieved. Will require review of spatial strategy within Core Strategy.	Regular monitoring by York Central Group. Dialogue between partner organisations and key stakeholders
Build Strong Communities	Improved Community Infrastructure	Failure to secure funds for Community Stadium	Fail to meet vision for community benefit.	Small project team established. Undertake S106 discussions to assess available capital-finalise development appraisals
Jobs and Economy	Unlocking infrastructure to support investment	Bring forward land for development	Inability to meet economic growth, increase in unemployment levels	Explore options and delivery vehicles for funding for York Central site and bring forward site
Jobs and Economy	supporting Business	changes in business support infrastructure, particularly due to revisions to Business Link	Confusion and duplication of advice to local businesses	Explore development of a web portal working with local partners

Jobs and Economy	supporting Business	Further downturn to international and global economies		council may need to amend economic development initiatives to respond to downturn rather than growth
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Communities and Neighbourhoods Risk Overview November 20

Annex B

Council Priority	Council outcome	Risk	Impact	Mitigations
Core Capabilities	A relentless focus on our priorities	Reduced funding	Job loses and cuts in services this will impact on customer satisfaction and staff morale. Levels of sickness may increase due to staff stress.	All managers are involved in reviewing services to cut out waste or increase income. Staff are updated with regards the current financial climate and asked to contribute ideas for remodelling services . Staff sickness is regularly reported and monitored. The Corporate Health and Wellbeing initiatives are available to staff
Core Capabilities	Deliver an ongoing Business Change Programme	Significant loss on Trading Accounts	Council's income is reduced which could result in further redundancies and service cuts and decline in customer satisfaction	Maintain partnership approach with major clients and continually improve cost effectiveness.
Core Capabilities	Health safety and well-being	Member of staff suffer a serious accident at work	Failure to ensure health and safety of staff in course of their duties could lead to increase in sickness or absence or the risk of legal action	Risk assessment carried out. Staff are made aware of safe working practices policies. Health and safety training is undertaken. Regular reporting and review of accidents is undertaken
Protect the Environment	Tackle Climate Change and reduce carbon omissions	Failure to achieve air quality targets	This risk concerns the ability of the Council to ensure that the air quality in certain areas of the city meets the health based air quality objective. Measures for the air quality action plan are not progressed across the council. This could result in an adverse impact on the council's reputation and the health of residents.	An Air Quality Action plan as a follow up to the Low Emission Strategy is to be produced and investigating whether low emission zones can be introduced.
Protect the Environment	Best Performing waste service	Failure to reduce waste going to landfill and increase recycling	The council will fail to meet its statutory targets for recycling and landfill diversion. Financial penalties may result as well as reputational risks.	Waste Strategy being developed including action plan for Zero Waste and the Waste minimisation Strategy. A PFI bid is progressing for the construction of a waste management facility ,Kerbside recycling project developed. Door stepping campaign commenced. Regular performance monitoring of performance targets

Protect Vulnerable People	Investing in services to support people in the community	Reduced funding for adaptations which results in Vulnerable customers put at risk by living in difficult and dangerous conditions	This puts additional pressure on already stretched resources as we will not be able to deliver timely and quality services leading to increase in complaints. Failure to provide this statutory service could result in reputational damage and negative media coverage, and we could be open to legal challenges. This also has a knock on effect to other services resulting in additional financial burden in areas such as nursing and residential care. The council has a duty to assess and make arrangements for adaptations via the chronically sick and disabled persons act 1970. The council also has mandatory duty to provide grants for adaptations via the Housing Grants Construction and Regeneration Act 1996. Lack of funding could prevent the council fulfilling its legal duties which could lead to a serious accident or fatality	Assessment framework in place to establish priorities for assistance Access to alternative support packages
Build Strong Communities	Community Engagement	New Neighbourhood working model is not accepted by the community	Increase in customer dissatisfaction and complaints. Adverse effect on reputation of the council. Resources are not targeted at those areas intended as the community may not have the necessary interest or skills to take on such responsibilities	Work alongside communities and partners to develop model and identify priorities to ensure understanding of roles and responsibilities. Learn lessons from the pilot and address in the new way of working. Working with CVS to develop volunteers and to assist in supporting the community. Staff located within community hubs to work alongside the community. Bringing together partners to delivery deliver plans in response to ward priorities. Provide clear channels for members to report issues and have them dealt with quickly. Neighbourhood Management support
Build Strong Communities	Safer Inclusive Communities	Failure to adhere to the requirements of the Single Equalities Act and implement the requirements of the act within prescribed timescales	The Council could be in breach of the requirements of legislation and inspection bodies. This can result in legal action, fines and poor inspection results. Failure to move from Achieving to Excellent for the Equalities Framework	Developing action plan to address the findings of the peer inspection and strengthen areas to move from achieving to excellent. Corporate commitment from ELG to DEL to Departmental Equality Networks. Equality Impact Assessment embedded in service and policy changes. Regular reporting on equality progress and issues
Build Strong Communities	Strong Voluntary Sector	review of grants and funding to the voluntary sector may result in some voluntary organisations not being eligible for council funding	Some voluntary organisations may not be able to continue to deliver services.	Ensure grant provision supports the priorities of the City Plan and Council Plan. Involve the voluntary sector in the review and have a adequate lead in times for the introduction of any changes so that those organisations who may not be eligible have an opportunity to bid for funds from other sources.



Audit and Governance Committee

5 December 2011

Report of the Assistant Director of Customer & Business Support Services (Financial Services)

Annual Audit Letter 2010/11 - Audit Commission**Summary**

1. This paper introduces the Annual Audit Letter 2010/11 (see annex A) prepared by the Audit Commission together with the council's response.

Background

2. The District Auditor reports annually his independent opinion of the Council's arrangements based on an annual programme of work agreed by officers and members. This programme of work must meet the standards set out in the Code of Audit Practice and gives an opinion on the corporate governance arrangements at the council focused across 3 main areas:
 - the opinion given on the council's annual Statement of Accounts (including the Annual Governance Statement);
 - assessment of arrangements to achieve value for money in the use of resources
 - to consider any matters brought to my attention by the public, and whether there is a need for the District Auditor to exercise his formal audit powers.
3. The Letter also provides details of the 2010/11 audit fee and a commentary from the Audit Commission on the current and future challenges facing the Council.

The council's response

4. The key messages contained in the Annual Audit Letter (AAL) which relate to the Financial Statements, were presented in detail to the Audit and Governance Committee on 29th September 2011 as part of the Annual Governance Report. The AAL notes the challenges for all authorities in implementing the requirements of the new International Financial Reporting Standards (IFRS), which was compounded at CYC by staffing changes resulting from organisational change. Although a number of amendments were made to the draft financial statements, none of the adjustments had any significant impact on the Council's underlying financial position and the District Auditor issued an unqualified opinion on the 2010/11 financial statements through the Annual Governance Report.

5. The AAL confirms that The Council has proper corporate arrangements in place to secure financial resilience, and to challenge how it delivered economy, efficiency and effectiveness (VFM) in the use of resources for 2010/11.. The Council's performance was assessed against criteria specified by the Audit Commission and arrangements were assessed adequate against each of the criteria. The AAL outlines the strengths and improvements identified by the Audit Commission. Specifically the Audit Commission has identified sustained strength in:
 - Medium Term Financial Planning;
 - Budget consultation with staff, stakeholders, local people and businesses;
 - An effective risk based approach to financial planning which has enabled the Council to plan to deliver a robust, balance budget without the need to reduce reserves or working balances;
 - Treasury management which continues to ensure investments deliver above average returns;
 - Effective financial reporting to Members;
 - Generally low service costs per head of population, low management and back office costs and low council Tax levels when compared to others;
 - Delivering efficiencies from already low cost base;
 - Staff suggestion scheme to foster a VFM culture and identify more opportunist operational savings;

- Good examples of shared service provision and outsourcing;
- Office relocation plans progressing well to secure significant financial savings;

The Letter does draw attention to some areas of activity which require close review;

- Most services are still delivered in-house and the Council may need to consider alternative models of service delivery in the future;
- Minimal investment in Council property over recent years, and asset records requiring improvement;
- An increased risk as a result of significant reductions in management and back office staff over recent years;
- A need to ensure that the Council is receiving value for money from its partnership activities.

6. In assessing the current and future challenges facing the Council, the AAL notes the steps that the Council has taken to maximise future funding streams including proactively marketing the services it can provide to partners and third parties. The report notes the need to keep under review the potential local impact of future changes to Housing Revenue Account financing, Council Tax Benefits subsidies and the localisation of NNDR arrangements. The Council has also requested the Audit Commission to undertake some Advice and Assistance work on asset management arrangements in the authority.

Consultation

7. Not relevant for the purpose of the report.

Options

8. Not relevant for the purpose of the report.

Analysis

9. Not relevant for the purpose of the report.

Corporate Priorities

9. This report contributes to the overall effectiveness of the council's governance and assurance arrangements.

Implications

10. There are no financial, HR, equalities, legal, crime and disorder, IT or property implications arising from this report.

Risk Management

11. By not responding effectively to the matters contained in this report, the council will fail to properly comply with legislative and best practice requirements.

Recommendations

12. Members are asked to:

- a) note the contents of this report and the Annual Letter itself, attached as the annex to this report;

Reason

To comply with the statutory requirements for the external audit of the council .

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**Report
Approved**



Date

Specialist Implications Officers

Not applicable

Wards Affected:

**AI
I**



For further information please contact the author of the report

Background Papers:

Annual Governance Report – Audit and Governance Committee 29th
September 2011

Annex

Annual Audit & Inspection Letter 2009/10

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Annual Audit Letter

City of York Council

Audit 2010/11



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Key messages

This report summarises the findings from my 2010/11 audit, which comprises two elements:

- the audit of your financial statements; and
 - my assessment of your arrangements to achieve value for money in your use of resources.
- I am also required to consider any matters brought to my attention by the public, and whether there is a need for me to exercise my formal audit powers.

Key audit risk	Our findings
Unqualified audit opinion	✓
Proper arrangements to secure value for money	✓
Certificate issued	✓

Value for money

The Council has a good track record of delivering efficiencies from an already low cost base. I have issued an unqualified conclusion stating that the Council had proper corporate arrangements in place to secure financial resilience, and to challenge how it delivered economy, efficiency and effectiveness in the use of resources for 2010/11.

Audit opinion on the financial statements

I have issued an unqualified opinion on the 2010/11 financial statements and my annual governance report was presented to Members on 29 September 2011.

A significant number of adjustments were made to the accounts originally presented for audit, but none of these had any significant impact on the Council's underlying financial position or levels of useable reserves and balances.

This is known as the value for money conclusion.

Audit certificate

I have not received any formal notices of objection from the public, and no other issues have arisen during our audit this year which required me to exercise my formal audit powers.

Consequently I was able to issue my certificate alongside the audit opinion on 29 September 2011.

Current and future challenges

Challenges	Key issues
<p>Economic downturn and financial pressure on the public sector</p>	<p>Financial plans have been reworked to reflect expected funding reductions in the next five years and deliver a balanced budget that maintains established levels of balances. Key changes approved for 2011-12 include:</p> <ul style="list-style-type: none">■ Focussing services on vulnerable people and those most in need■ Reducing the cost of management and back office services■ Reducing expenditure following government reductions to specific grants.
<p>Future funding streams</p>	<p>The Council has developed a good track record of delivering to budget in recent years but there are continued pressures on specific service areas such as social care and looked after children which will continue to need careful management. It is also likely that the scale of spending reductions required in future years will require local authorities to adopt more strategic solutions. The Council has some examples of shared service provision and plans for a joint waste disposal facility are well underway, but most services are still delivered in-house and the Council may need to consider alternative models of service delivery in the future.</p>
<p>Asset Management</p>	<p>The Council has taken appropriate steps to maximise future funding streams. Fees and charges are kept under regular review. The Council has also reconsidered the future of several areas of expenditure in the light of reductions to specific grant funding schemes, and is more proactively marketing the services it can provide to partners and third parties. But proposed changes to Housing Revenue Account financing, housing benefits subsidies and NNDR pooling arrangements could all have a significant impact on local authority finances in future years. The potential impact of these at a local level will need to be kept under review and assessed as part of future budget preparations.</p>
<p>Asset Management</p>	<p>Well-planned asset management can improve public services, reduce costs and generate additional income. We reported on the Council's approach to asset management in December 2009 and made a number of recommendations for improvement. Some progress has been made and the move to new office accommodation next year should secure significant financial savings as well as improved facilities for customers and staff. Further action is necessary however as there has been minimal investment in Council property over recent years, and a somewhat fragmented approach. The Council has asked us to review asset management as Advice and Assistance work and our findings will be reported to</p>

Challenges	Key issues
Treasury management	<p>Members early in 2012.</p> <p>Treasury management strategies and policies, in particular judgements about the sums set aside to meet future repayments of debts, have a significant impact on the Council's finances. The Council has achieved above average rates of return on its investments in future years but to help meet future financial challenges it intends to review treasury management strategies and set aside arrangements in the coming year. Any such changes should be properly approved by members, and supported by a comprehensive review of not just strategic objectives and policies but also the supporting capital financing calculations.</p>
Implementing International Financial Reporting Standards	<p>Meeting new reporting requirements has been challenging for all authorities and the financial statements submitted for audit required significant adjustment. We are already discussing with Council officers how the closedown processes can be better managed next year with a view to:</p> <ul style="list-style-type: none"> • allowing sufficient time for preparation and audit of both the accounts and Whole of Government return by the due dates. • strengthening internal review so that obvious errors and inconsistencies are eliminated prior to audit.

Financial statements and annual governance statement

The Council's financial statements and annual governance statement are an important means by which the Council accounts for its stewardship of public funds.

Overall conclusion from the audit

Implementing the new requirements of International Financial Reporting Standards, which had full retrospective effect, was a challenging process for all local authorities in 2010/11. At City of York Council this challenge was compounded by staffing and organisational changes. Consequently a significant number of amendments were made to the financial statements originally presented for audit:

- The Cash Flow Statement, Movement in Reserves Statement, segmental analysis and restatement of prior years' balances were all significantly reworked following our initial review and officers' own reflections on the accounts and reporting requirements
- Additional disclosures were made in the Housing Revenue Account, together with reclassification and analysis of investment property transactions, grant income and cash and cash equivalents
- Errors in relation to pension changes and property, plant and equipment transactions were corrected together with a number of other, more minor amendments to improve the presentational aspects of the financial statements and internal consistency between core statements and disclosure notes.
- The explanatory foreword was also amended as a consequence of the above changes to the accounts.

Fortunately none of these adjustments had any significant impact on the Council's underlying financial position or levels of useable reserves and reserves.

Significant weaknesses in internal control

The only internal controls I considered during the course of the audit were those relevant to my opinion on the financial statements. External audit work is not designed, and should not be relied upon, to identify all the weaknesses in internal control that might exist.

Any internal control issues identified by us, together with suggestions for improvement, were included in my regular progress reports to Members during the year. I have undertaken additional procedures where necessary to compensate for any weaknesses in internal control which are relevant to the audit. My conclusion for 2010/11 was that the Council's financial systems overall were adequately controlled, but that improvement was needed in two specific areas:

- problems with completing timely bank reconciliations were highlighted last year. These have largely been addressed through compensating controls within the relevant financial systems, and by reconciling various components of the bank reconciliation at different points during the year. However a full bank reconciliation covering daily cash records, bank statements and all relevant general ledger account codes was only carried out at the year end. We have recommended that in future this is undertaken on a quarterly basis.
- the Framework 1 system, which is used to record approved social care contracts, was not regularly reconciled to the general ledger during the year and it appears that the operation and evidencing of some detailed processing controls has changed without specific authorisation by management.

Whole of Government Accounts

Whole of Government Account returns are an important part of the Government's national financial management framework, and submission deadlines were brought forward this year. The Council did not submit its 2010/11 data on time and this meant that we in turn were unable to meet our target date of 30 September 2011 for completing and reporting on our audit work. I gave an unqualified opinion on the return on 14 October.

The Council should plan and manage its closedown processes in future years to allow sufficient time for both the preparation and audit of the Whole of Government Accounts pack by the national deadline dates.

Value for money

I considered whether the Council is managing and using its money, time and people to deliver value for money. I assessed your performance against the criteria specified by the Audit Commission and have reported the outcome as the value for money conclusion.

I assess your arrangements to secure economy, efficiency and effectiveness in your use of resources against two criteria specified by the Audit Commission. To help inform this assessment I have followed up recommendations from previous years' work and reports, and specific issues highlighted by continuous audit planning and the Council's own risk management processes. In 2010/11 this included consideration of:

- Asset management
- Corporate efficiency programmes
- corporate and finance function restructuring
- office relocation plans
- the joint waste PFI scheme
- partnership governance arrangements, particularly for demonstrating and reporting on value for money.

My overall conclusion is that the Council had proper arrangements in place, and my findings in respect of each of the two specific criteria are summarised below.

Value for money criteria and key messages

Criterion	Key messages
1. The organisation has proper arrangements in place to secure financial resilience.	Criteria met. The Council has adopted an integrated process for updating the medium term financial plan and

Criterion

Focus for 2010/11:

The organisation has robust systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future.

Key messages

setting annual budgets. Both have been significantly reworked in the light of the Government's spending review and reflect anticipated reductions to funding levels of over coming years. Extensive consultation with staff, stakeholders, local people and businesses has enabled the Council to revisit its priorities and a series of reports to members, staff newsletters and public meetings have taken place to ensure that the Council's financial position is clearly and widely understood. Key changes approved for 2011-12 include:

- Focussing services on vulnerable people and those most in need
- Reducing the cost of management and back office services
- Reducing expenditure following government reductions to specific grants.

Members have played their full part in this debate, and draft budgets were subject to detailed review by portfolio holders and Executive before finalisation and Full Council approval.

Financial plans clearly set out the key risk areas and how these will be managed, and make reasonably prudent assumptions about funding levels, interest rates, pay and price increases. Plans indicate that the Council is intending to deliver a balanced budget going forward without significant reductions to reserves and working balances, which have been maintained at £6.1m in line with Council policy.

The Council has developed a good track record of delivering to budget in recent years. Pressures on budgets in specific service areas such as social care and looked after children are now promptly identified and tackled. Treasury Management is also sound, with no statutory breaches or impairment losses reported in 2010-11 and above average rates of return. Quarterly reports to members are comprehensive and comprehensible, providing forecast outturn as well as year to date. More centralised financial management arrangements are being put in place for 2011-12 to implement a more standardised approach to budget setting and monitoring between Council departments.

Criteria met.

The Council has generally low service costs per head of population, low management and back office costs and low Council Tax levels, when compared to others. Performance reports, scrutiny reviews and other reports to members contain comparative information so there is generally a sound awareness of how costs and quality of service compare with others.

2. The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.

Focus for 2010/11:

Criterion

The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and by improving efficiency and productivity.

Key messages

There is a good track record of delivering efficiencies from an already low cost base. An ongoing efficiency programme looks to identify and deliver savings, based on comparing the Council to "best in class". A staff suggestion scheme is also in place to foster a value for money culture and identify more opportunist operational savings. There are some examples of shared service provision and outsourcing, and plans for a joint waste PFI scheme are well underway. Most services are still delivered in-house however and the Council may need to consider alternative models of service delivery in the future.

Most support services have now been centralised, area based service delivery and more homeworking for revenues and benefits staff are also helping to reduce costs. Fees and charges are regularly reviewed and services the Council can provide to partners and third parties are pro-actively marketed.

Office relocation plans are progressing well, and should secure significant financial savings as well as improved facilities for customers and staff. However there has been minimal investment in Council property over recent years, and asset records require improvement.

A significant number of management and back office posts have been taken out of the establishment over recent years. This has reduced costs but also in some areas increased risk. For example now that the central partnership team has been wound up it is not clear how the Council will ensure that it is receiving value for money from partnerships.

Closing remarks

This letter has been discussed and agreed with the Chief Executive and the Director of Customer and Business Support Services, and will be presented to the Audit and Governance Committee on 5 December 2011. Copies will be provided to all elected members.

Detailed findings, conclusions and recommendations in the areas covered by our audit have been included in the following reports which I have issued during the year.

Report	Date issued
Initial Fee Letter	April 2010
Opinion Audit Plan	February 2011
Audit Progress Reports	April and July 2011
<ul style="list-style-type: none">Annual Governance ReportAudit opinion , certificate and value for money conclusion	September 2011
Whole of Government certification and assurance statement	October 2011
Annual Audit Letter	November 2011

The Council has taken a positive and constructive approach to our audit, and I would like to thank the Council's staff for their support and co-operation.

Steve Nicklin

District Auditor

November 2011

Appendix 1 - Fees

	Actual	Proposed	Variance
Audit Fee (1)	£248,900	£248,900	0
Mandated work – National Fraud Initiative	£3,650	£3,650	0
Grant claims and returns (2)	£42,700	£42,700	0
Total (3)	£295,250	£295,950	0

1. The Audit Commission scale fee for York City Council is £249,260.
2. This represents our current best estimate for grant claims and returns fees. The work is not likely to be completed until the end of December 2011.
3. The figures above do not reflect the fee rebates made to audited bodies on a national basis as a result of savings made by the Audit Commission. The rebate received by City of York Council in 2010-11 was £15,576.

Appendix 2 - Glossary

Annual governance statement

Governance is about how local government bodies ensure that they are doing the right things, in the right way, for the right people, in a timely, inclusive, open, honest and accountable manner.

It comprises the systems and processes, cultures and values, by which local government bodies are directed and controlled and through which they account to, engage with and where appropriate, lead their communities.

The annual governance statement is a public report by the Council on the extent to which it complies with its own local governance code, including how it has monitored the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.

Audit opinion

On completion of the audit of the financial statements, I must give my opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question; and
- whether they have been prepared properly, following the relevant accounting rules.

Opinion

If I agree that the financial statements give a true and fair view, I issue an unqualified opinion. I issue a qualified opinion if:

- I find the statements do not give a true and fair view; or
- I cannot confirm that the statements give a true and fair view.

Value for money conclusion

The auditor's conclusion on whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of resources based on criteria specified by the Audit Commission.

If I find that the audited body had adequate arrangements, I issue an unqualified conclusion. If I find that it did not, I issue a qualified conclusion.

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- any director/member or officer in their individual capacity; or
- any third party.





Audit and Governance Committee

5 December 2011

Report of the Assistant Director Financial Services

**Review of the Effectiveness of the System of Internal Audit
2011/12****Summary**

1. To agree the arrangements for the 2011/12 review of the effectiveness of internal audit.

Background

2. The Accounts and Audit Regulations 2011 require each local authority to conduct an annual review of the effectiveness of its internal audit, and to report the findings of this review to an appropriate committee. The process is intended to form part of the wider review of the effectiveness of the system of internal control (required to prepare the Annual Governance Statement - AGS).
3. Best practice guidance issued by the Chartered Institute of Public Finance (CIPFA) also recommends that audit committees should periodically review their own effectiveness so as to ensure that they continue to properly fulfil their responsibilities.
4. For 2010/11, the annual review of the effectiveness of internal audit was undertaken jointly with the North Yorkshire County Council by the Shared Service Contract Board (SSCB), and in consultation with the respective Audit Committee chairs. The SSCB comprises the respective client officers from the City of York and the County Council, and Veritau's Head of Internal Audit. Meetings of the SSCB are held approximately six times a year and involve consideration of performance indicators, changes in working practices and other service developments.

The results of the 2010/11 review were reported to this Committee on 28 June 2011.

5. Earlier this year, CIPFA undertook a survey of heads of internal audit to assess the current arrangements for audit committees in local government. The results of the survey were published in May 2011 and reported to this Committee on 30 June 2011. CIPFA are now using the findings of the survey to develop further guidance and support to audit committees. It is also recognised that the role of audit committees may change in the future as a result of the government's proposals for the future of public audit and the expectation that local authorities will be given responsibility for the appointment of their own external auditors. The consultation period ended on 30 June 2011 but it is not yet known when the final plans for external audit arrangements will be published.

Proposed Arrangements for 2011/12

6. The Regulations require either the Council itself or a committee of the Council to review the effectiveness of internal audit, and for the review to be performed annually. The Council has delegated this responsibility to the Audit and Governance Committee and included it within the terms of reference for the Committee. To ensure consistency and avoid unnecessary duplication, it is proposed that the SSCB should again undertake the detailed work, with the process overseen by the chair of the Audit and Governance Committee. As last year, it is proposed that the outcome of the review will then be reported to the June 2012 meeting of this Committee.
7. The best practice guidance states that the review of the effectiveness of internal audit should also include consideration of the effectiveness of the Audit and Governance Committee itself (to the extent that its work relates to internal audit) as well as the performance of the audit provider. The Audit and Governance Committee has not reviewed its own effectiveness, and this will be an action to undertake during 2011/12

Options

8. Not relevant for the purpose of the report.

Corporate Priorities

9. This report contributes to the council's overall aims and priorities by helping to ensure probity, integrity and honesty in everything it does. It also contributes to the improving Effective Organisation corporate priority.

Implications

10. The implications are;
 - **Financial** – there are no financial implications to this report.
 - **Human Resources (HR)** – there are no HR implications to this report.
 - **Equalities** - there are no equalities implications to this report.
 - **Legal** - there are no legal implications to this report
 - **Crime and Disorder** – there are no crime and disorder implications to this report.
 - **Information Technology (IT)** - there are no IT implications to this report.
 - **Property** - there are no property implications to this report.

Risk Management Assessment

11. The Council will fail to comply with the Accounts and Audit Regulations if it does not undertake an annual review of the effectiveness of internal audit, as part of the wider review of the effectiveness of the system of internal control.

Recommendation

12. Members are asked to agree the proposed review arrangements for 2011/12

Reason

To enable Members to consider the adequacy and effectiveness of the council's control environment.

Contact Details

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Services
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Ian Floyd
Director of Customer & Business
Support Services

**Report
Approved**



Date 17.11.11

Specialist Implications Officers

Not applicable

Wards Affected: Not applicable



For further information please contact the author of the report

Background Papers

CIPFA Better Governance Forum – Audit Committee Update issue
5



Audit and Governance Committee

5 December 2011

Report of the Assistant Director, Financial Services

Audit, Counter Fraud & Information Governance Monitoring Report

Summary

- 1 This report provides an update on progress made in delivering the internal audit workplan for 2011/12 and on current counter fraud and information governance activity. The report also includes details of a proposed expansion of Veritau in order to allow the company to provide internal audit services to a number of North Yorkshire district councils.

Background

- 2 The work of internal audit is governed by the Accounts and Audit Regulations 2011 and the CIPFA Code of Practice for Internal Audit in Local Government. In accordance with the code of practice, the 2011/12 audit and fraud plan was approved by the Audit and Governance Committee on 19 April 2011. The plan included a programme of audit reviews, together with details of planned counter fraud and information governance activities.
- 3 This report provides an update on work undertaken against the approved plan.

2011/12 Internal Audit Plan – Progress to Date

- 4 Two of the priorities for Veritau are to deliver at least 93% of the audit plan and to ensure that the service continues to operate to recognised professional standards (as determined by the Code of Practice).
- 5 Internal audit successfully delivered 95.3% of the 2010/11 audit plan. To date, 37% of the 2011/12 audit plan has been

completed (compared to 37% at the same point last year). This figure is based on reports issued and does not take into account further audit fieldwork which has been completed. It is anticipated that the 93% target will be exceeded by the end of April 2012 (the cut off point for 2011/12 audits). Details of the audits completed and reports issued since the last report to this committee in September 2011 are given in annex 1.

- 6 There have been no variations to the audit plan since the last report in September.

Counter Fraud

- 7 Counter fraud work has been undertaken in accordance with the approved plan. Annex 2 provides details of the investigations completed to date and provides a summary of the work undertaken.

Information Governance

- 8 The team provides ongoing support and advice to service departments in managing information governance issues. This includes measures to reduce the risk of data security breaches.
- 9 So far this year (to 31 October) the team has received and tracked 479 Freedom of Information requests, up from 378 in the same period last year (a 27% increase).

Breaches of Financial Regulations

- 10 Only one minor breach of the council's financial regulations has been identified since the last report to this committee. This related to issues around the maintenance of inventory records.

Integration with North Yorkshire Audit Partnership

Background

- 11 Veritau Limited was originally formed on 19 January 2009. On 1 April 2009, the council and North Yorkshire County Council (NYCC) transferred their internal audit, counter fraud and information governance services to the new company. From this date, Veritau has been contracted to provide these services to the two councils together with a number of other

public sector bodies. The company is wholly owned by the council and NYCC, with each holding 50% of the share capital.

- 12 Veritau currently employs approximately 35 staff, organised into five teams. In addition, both the council and NYCC second staff to the company in support of their own professional training programmes (normally CIPFA or AAT). The company operates from two offices, one in York and the other at County Hall, Northallerton.
- 13 The North Yorkshire Audit Partnership (NYAP) was formed in February 1999. The partnership originally consisted of Scarborough Borough, Selby District and Ryedale District Councils. Richmondshire and Hambleton District Councils joined the partnership in May 2008. The partnership is based on a joint committee model with Ryedale District Council acting as lead authority. The existing partnership agreement ends on 31 March 2012.
- 14 NYAP currently employs 12 staff and provides internal audit and counter fraud services to the five partner councils. The staff are employed by Ryedale DC and the service is delivered via satellite offices at each council.
- 15 The NYAP Directors approached Veritau in November 2009 to discuss potential options for future collaboration. These discussions showed that there was a high level of interest in the possibility of the existing services provided by NYAP being transferred to Veritau. Details of the outline proposals were presented to this committee on 6 December 2010. Since that date, detailed plans have been developed to address the legal, financial, staffing and operational implications of any such transfer. Various options for the structure of the expanded business have also been considered, including increasing the number of shareholders in Veritau or establishing a subsidiary company. Details of the final proposals are set out below.

Drivers for Change

- 16 The NYAP member councils are facing similar challenges to the council in terms of delivering internal audit and counter fraud services at a time of financial pressures and significant

change. The main drivers for change are therefore the need to:

- deliver further efficiencies and cost savings
- ensure future service resilience and capacity so as to be able to respond to changing priorities and increasing workload demands
- retain skilled and experienced staff by creating greater critical mass and providing more opportunities for career development and specialism
- make best use of the scarce professional audit expertise available (particularly in contract and IT audit)
- establish an effective succession plan and to reduce the existing reliance on certain key staff for service continuity (particularly within NYAP).

Detailed Proposals

- 17 It is proposed that the services currently provided by NYAP to the 5 district councils are transferred to Veritau on 1 April 2012. Staff currently employed in providing those services would then transfer to Veritau in accordance with the Transfer of Undertakings (Protection of Employment) Regulations (TUPE).
- 18 Veritau will form a subsidiary company called Veritau – North Yorkshire Limited (VNY) to deliver the transferring services. The subsidiary company will be limited by shares with Veritau holding 50% of the share capital and each district council holding 10%. The subsidiary company will have a board of directors comprising an officer from each district council and two directors appointed by Veritau.
- 19 The creation and future operating arrangements of the subsidiary company will be governed by a formal shareholders agreement. The agreement will set out the rights and obligations of the shareholders and the ongoing relationship between each council and Veritau as participants in the venture. The services to be provided to each district council will be specified in separate service agreements, identical or similar to the existing service agreements which Veritau currently has with the council and NYCC. The length of the

new service agreements would be coterminous with Veritau's existing service agreements.

- 20 Each district council will nominate a client officer to oversee the delivery of services under its service agreement with VNY. The annual fee for the core service will be calculated on the basis of an agreed daily fee rate, multiplied by the agreed level of service i.e. the number of days required by each district council. The daily fee rate will be same for each district council and the rate charged by Veritau to the council and NYCC. Each district council will however be able to request additional work under its service agreement. The fee for such additional work will be calculated on the basis of rates for additional work for the appropriate grade of staff which will be specified in the relevant service agreement.
- 21 Each district council will provide serviced office accommodation on similar terms to the existing arrangements Veritau has with the council and NYCC.
- 22 Veritau will seek to ensure that the transferring staff are included in the Local Government Pension Scheme. Staff will also be given the option of transferring from their existing terms and conditions to those of VNY (which will be identical to those offered by Veritau).
- 23 The new company would be a separate legal entity but, as far as possible, the Veritau 'group' would operate as a single entity with common systems, working practices and one overall management structure. Specific governance rules will also be established to ensure that the two companies in the Veritau 'group' operate and take decisions in the context of a common understanding and shared vision. To ensure effective communication between the two boards of directors, copies of agendas and minutes of meetings will be circulated between each. In addition, at least one of the directors appointed to the board of VNY will also be a director of Veritau Limited.
- 24 The Veritau management team will be responsible for all aspects of VNY's operational management. The specific responsibilities of the Board of Directors and the management team will be set out in a scheme of delegation (similar to the one adopted for Veritau). Transfer pricing arrangements need be established between the two companies to reduce the risk

of challenge by HMRC but these will be kept simple to avoid any unnecessary additional administrative burden.

- 25 A draft budget has been prepared for the Veritau 'group'. The budget reflects the economies of scale which will be possible by operating an expanded business. For 2012/13, the proposed daily fee rate for internal audit and counter fraud services to the district councils will be £225¹. The fee represents a reduction of 4.3% on the existing fee rate chargeable by NYAP. It is also proposed that the daily fee rate charged by Veritau to the council and NYCC will be reduced to £225 in line with this revised rate. This will represent a saving to the council of approximately £13k pa (2.0%) on existing fees.
- 26 Veritau has a contract with PricewaterhouseCoopers (PWC) for the provision of specialist computer audit services. These services will be made available to the district councils on request but would be recharged at cost.
- 27 Set-up costs will be incurred as a result of the creation of VNY and the transfer of services from NYAP. These costs will include the provision of legal advice, additional licences for IT applications and support to staff through the change process. It is estimated that these costs will be approximately £16k. It is proposed that the actual set-up costs will be shared 50/50 between Veritau and NYAP. Veritau's share of the set-up costs together with an initial capital contribution of £10k will be met from the company's reserves. It is also recognised that NYAP will incur some expenditure in winding up the partnership, for example, the costs of any redundancies. These costs will be met from the partnership's reserves.
- 28 The existing support service arrangements (legal, IT, finance, HR and payroll) which are currently provided to Veritau by the Council and NYCC will be extended to include VNY.
- 29 A detailed action plan has been prepared to complete the implementation process. Subject to approval, a project board comprising officers from Veritau and NYAP will oversee the set up of VNY and complete the transfer of services and employees to the new company.

Benefits

¹ This assumes that there is no increase in the JNC national pay rate for 2012/13.

- 30 The key benefits of the proposal to the council and NYCC as shareholders in Veritau are that it will:
- help achieve greater critical mass and hence provide scope to further improve the resilience and capacity of the existing services provided by Veritau
 - deliver cost savings to the council and NYCC. These cost savings will be achieved by sharing overheads, reducing unproductive time and greater economies of scale
 - further enhance the focus on service delivery, professionalism and quality
 - further increase the opportunity for staff to specialise as well as enhancing career opportunities, resulting in greater staff satisfaction and retention
 - further reduce reliance on key members of staff for service continuity
 - enable the council and NYCC to retain full control of Veritau (whilst offering the district councils influence over VNY)
 - avoid the need for the council and NYCC to value their existing shareholding in Veritau and for the district councils to purchase a proportion of the shares
 - avoid any risk to the council's investment in Veritau should VNY encounter future financial or operational difficulties. Veritau could continue trading even if the wider 'partnership' failed
 - offer greater transparency since the different parts of the business will be trading as separate entities.
- 31 The proposed structure of the expanded business is considered less likely to be subject to challenge under EU public procurement legislation (Teckal) compared to granting the district councils a minority shareholding in Veritau itself. The approach also offers a model for any further expansion of the company, for example to accommodate other future public sector partner organisations.

Timetable

- 32 The district councils have already obtained approval from their respective member decision making bodies to wind-up NYAP and to transfer their internal audit and counter fraud services to Veritau on 1 April 2012. Formal approval to the proposed expansion of Veritau however still needs to be obtained from both the council and NYCC (as Veritau's existing shareholders).
- 33 Details of the proposals are due to be presented NYCC's Executive on 20 December 2011 and the Cabinet on 10 January 2012.
- 34 Details of the outline timetable necessary to establish VNY are set out below:

Action	Target Date for Completion
Formal consultation with NYAP staff to be completed	31/12/2011
Staffing establishment in VNY to be confirmed	15/1/2012
Pension admission agreement to be finalised	31/1/2012
Company formation and issue of share capital	31/1/2012
Appointment of directors to the board of VNY	31/1/2012
Legal agreements to be finalised	28/2/2012
Client officers to be appointed	28/2/2012
Business Plan (3 year) to be approved by board of VNY	15/3/2012
2012/13 budget to be approved by board of VNY	15/3/2012
Formal transfer of services and staff to VNY	1/4/2012

Consultation

- 35 Not relevant for the purpose of the report.

Options

36 Not relevant for the purpose of the report.

Analysis

37 Not relevant for the purpose of the report.

Corporate Priorities

38 This report contributes to the council's overall aims and priorities by helping to ensure probity, integrity and honesty in everything it does.

Implications

39 There are no implications to this report in relation to:

- **Finance**
- **Human Resources (HR)**
- **Equalities**
- **Legal**
- **Crime and Disorder**
- **Information Technology (IT)**
- **Property**

Risk Management Assessment

40 The council will fail to properly comply with the CIPFA Code of Practice for Internal Audit in Local Government if the results of audit work are not reported to those charged with governance.

Recommendation

41 Members are asked to:

- (a) Note the progress made in delivering the 2011/12 internal audit work programme, and current counter fraud and information governance activity.

Reason

To enable members to consider the implications of audit and fraud findings.

- (b) Comment on the proposals to establish a subsidiary company (Veritau North Yorkshire) to undertake work transferred from the North Yorkshire Audit Partnership, prior to consideration of the proposals by the Cabinet.

Reason

As part of the committee's responsibility to consider reports dealing with the management of internal audit

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**Report
Approved**



Date 22/11/11

Specialist Implications Officers

Not applicable

Wards Affected: Not applicable

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For further information please contact the author of the report

Background Papers

- 2011/12 Internal Audit & Counter Fraud Plan
- NYAP Integration Report and Action Plans

Annexes

Annex 1 – 2011/12 Audits Completed and Reports Issued
Annex 2 – Counter Fraud Activity

AUDITS COMPLETED AND REPORTS ISSUED

The following categories of opinion are used for audit reports.

Opinion	Level of Assurance
High Assurance	Overall, very good management of risk. An effective control environment appears to be in operation.
Substantial	Overall, good management of risk with few weaknesses identified. An effective control environment is in operation but there is scope for further improvement in the areas identified.
Moderate	Overall, satisfactory management of risk with a number of weaknesses identified. An acceptable control environment is in operation but there are a number of improvements that could be made.
Limited	Overall, poor management of risk with significant control weaknesses in key areas and major improvements required before an effective control environment will be in operation.
No Assurance	Overall, there is a fundamental failure in control and risks are not being effectively managed. A number of key areas require substantial improvement to protect the system from error and abuse.

Actions to address issues are agreed with managers where weaknesses in control are identified. The following categories are used to classify agreed actions.

Priority

Long Definition

Short Definition – for use in Audit Reports

1 (High)

Action considered both critical and mandatory to protect the organisation from exposure to high or catastrophic risks. For example, death or injury of staff or customers, significant financial loss or major disruption to service continuity.

These are fundamental matters relating to factors critical to the success of the area under review or which may impact upon the organisation as a whole. Failure to implement such recommendations may result in material loss or error or have an adverse impact upon the organisation's reputation.

A fundamental system weakness, which presents unacceptable risk to the system objectives and requires urgent attention by management.

Priority

Long Definition

Short Definition – for use in Audit Reports

	<p>Such issues may require the input at Corporate Director/Assistant Director level and may result in significant and immediate action to address the issues raised.</p>	
2	<p>Action considered necessary to improve or implement system controls so as to ensure an effective control environment exists to minimise exposure to significant risks such as financial or other loss.</p>	<p>A significant system weakness, whose impact or frequency presents risks to the system objectives, and which needs to be addressed by management.</p>
	<p>Such issues may require the input at Head of Service or senior management level and may result in significantly revised or new controls.</p>	
3	<p>Action considered prudent to improve existing system controls to provide an effective control environment in order to minimise exposure to significant risks such as financial or other loss.</p>	<p>The system objectives are not exposed to significant risk, but the issue merits attention by management.</p>
	<p>Such issues are usually matters that can be implemented through line management action and may result in efficiencies.</p>	

Draft Reports Issued

9 internal audit reports are currently in draft. These reports are with management for consideration and comments. Once the reports have been finalised, details of the key findings and issues will be reported to this committee. The draft reports are categorised as follows:

Opinion	Number
"High Assurance"	5
"Substantial Assurance"	1
"Moderate Assurance"	0
"Limited Assurance"	0
"No Assurance"	0
"Not given"	3

Final Reports Issued

The table below shows audit reports finalised since the last report to this committee in September 2011. In all cases the recommendations made have been accepted by management, and will be followed up by internal audit.

Audit	Date Of Final Report	Opinion	Number of Agreed Actions		Work done / significant weaknesses / issues identified
			Total	Priority 1	
Stockton On The Forest Primary School	7/10/11	High Assurance	3	0	A school audit. No significant issues were identified.
Bishopthorpe Infant School	17/10/11	High Assurance	4	0	A school audit. No significant issues were identified.
York High School	20/10/11	High Assurance	2	0	A school audit. No significant issues were identified.
Information Security Checks at the Eco Depot	3/11/11	None Given	NA	NA	An unannounced spot check on offices at the Eco Depot. The purpose of this visit was to assess the extent to which data security is being considered by staff in ensuring that confidential, personal or sensitive data is stored securely. The audit looked at hard copy documents as well as digital storage such as laptops and removable media. This followed a similar exercise conducted at various city centre council offices in March for which the findings were reported

Audit	Date Of Final Report	Opinion	Number of Agreed Actions		Work done / significant weaknesses / issues identified
			Total	Priority 1	
					separately. No significant concerns were identified and overall information security in these offices seems to be good. There were some specific issues identified and these have been reported to the relevant managers.
Carr Infant School	15/11/11	High Assurance	2	0	A school audit. No significant issues were identified.

COUNTER FRAUD ACTIVITY 2011/12

The table below shows the total numbers of fraud referrals received and summarises the outcomes of investigations completed. While benefit fraud is still a major role for the team, there is a continuing increase in the work the team undertakes in other areas. The indicators have been updated from previous years to reflect this and now include the full range of counter fraud work undertaken.

	2011/12 (as at 31/10/11)	2011/12 (Target: Full Yr)	2010/11 (Actual: Full Yr)
Number of Fraud referrals received. <i>The target is designed to promote fraud awareness and encourage people to report suspected fraud.</i>	397	400	456
% of investigations completed which result in a successful outcome (for example benefit stopped or amended, sanctions, prosecutions, properties recovered, housing allocations blocked, management action taken). <i>The target is designed to measure the effectiveness of counter fraud activity</i>	33%	30%	62%
Value of fraudulent benefit overpayments identified. <i>The target is designed to measure the effectiveness of counter fraud activity</i>	£362k	£350k	£390k
Number of investigations completed	220	N/A	266 ¹

¹ The comparative figure for 2010/11 has been restated from that previously reported, to exclude Housing Benefit Matching Service (HBMS) cases. This enables fraud referrals and outcomes to be considered on a like for like basis.

Number of successful outcomes ²	73	N/A	53
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There has been a significant increase in the value of fraudulent benefit overpayments identified in the year to date (£362k) compared to last year (£209k) and the increase in the last two months is of particular note (up from £238k at the end of August). It is difficult to attribute specific underlying reasons for this. A large number of cases have reached a conclusion in the period and therefore it may be partly due to timing issues. However, there are also some indications that the periods over which fraud is committed are increasing. Approximately a third of the increase in overpayments since August is attributable to one case (£36k) which covered a period of ten years.

Caseload figures for the period are:

	As at 1/4/11	As at 31/10/11
Awaiting allocation	91	93
Under investigation	259	211

Summary of counter fraud activity:

Activity	Work Completed or in Progress
Data Matching	<p>Investigation of National Fraud Initiative cases is still ongoing. A total of 1,330 recommended matches were highlighted by the Audit Commission in their latest exercise.</p> <ul style="list-style-type: none"> Concessionary travel passes - 559 of the matches related to concessionary travel passes. These have been reviewed by the service department and 188 passes have been withdrawn as a result. There is, however, no indication of fraud. The matches result from a comparison

² 2011/12 figures will be higher than previous years as it includes all successful outcomes rather than just benefit related sanctions and prosecutions.

Activity	Work Completed or in Progress
	<p>of passes issued to deceased persons. Nearly all of the remaining 371 matches were similar in nature, but the death had already been notified to the council and the pass withdrawn (i.e. the council were notified after the date of the original data extract).</p> <ul style="list-style-type: none"> • Other matches - the remaining 771 matches cover a range of areas. 655 have been reviewed by Veritau to date. None of the matches highlight any fraud and only 5 errors were identified as a result of the matches (only one error has a value attached of £3.4k). A further 116 matches remain to be looked at. <p>Housing Benefit Matching Service (HBMS) referrals continue to be investigated - the counter fraud team has received 579 HBMS referrals to date in 2011/12.</p>
Fraud Detection and Investigation	<p>In addition to benefit fraud investigation, the service continues to promote the use of criminal investigation techniques and standards in other areas to encourage a robust response to any fraud perpetrated against the council. Activity to date includes the following.</p> <ul style="list-style-type: none"> • Benefit Fraud - 15 people have been prosecuted for benefit fraud offences and a further 17 have received formal sanctions (cautions and administrative penalties). Benefits have been corrected in a further 28 cases. • Housing Fraud – ten housing fraud cases have resulted in houses being freed up for letting. Four properties were recovered from existing tenants. A further six properties were

Activity	Work Completed or in Progress
	<p>prevented from being let where the prospective tenants had provided fraudulent information in their housing application. The council's success in recovering properties in 2010/11 was also highlighted in the recent Audit Commission <i>Protecting the Public Purse 2011</i> report</p> <ul style="list-style-type: none"> • Internal Fraud - the team has investigated nine internal frauds during the year. • Blue Badge Fraud – one case has been completed, and resulted in a caution being issued. A second case is in progress.



Audit & Governance**5 December 2011**

Report of the Cabinet Member for Corporate Services

Scrutiny of Treasury Management Monitor 2 Mid year Review and Prudential Indicators 2011/12**Summary**

1. The Audit & Governance Committee are responsible for ensuring effective scrutiny of the treasury management strategy and policies. The revised Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance (“the Code”) stipulated that
 - There needs to be, at a minimum, 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,
 - Those charged with governance are also personally responsible for ensuring they have the necessary skills and training
2. Attached at Appendix A is the Treasury Management Monitor 2 Mid Year Review and Prudential Indicators 2011/12 report. This information provides Members with an update of treasury management activity for the first six months of 2011/12.

Background

3. The report reviews the economic market conditions in which the treasury management activities of the council are currently operating. It highlights that the bank base rate will remain low for the foreseeable future with quarter 3 of 2013 being estimated as the first time the base rate will rise.
4. Investment rates remain low and the counterparty list, where the council’s surplus funds can be invested, is limited due to the uncertainty surrounding the euro zone and the impact on world market. This ensures the security of the Councils capital, with the secondary priority being on interest rate return predicted at 1.5% for 2011/12.

5. Borrowing rates are continually being monitored due to the current volatility in the market creating some good opportunities to take loans at favourable rates. The target borrowing rate in 2011/12 is currently 4.3% and loans taken this year are below the target.
6. In addition, the report highlights the proposed reform of the HRA subsidy arrangements. A one-off payment will be made to the government in March 2012 and this creates the requirement for additional borrowing. The details of the HRA reform are included in Appendix A which explains the need for full council approval of the change in the prudential indicators and treasury management strategy for 2011/12.
7. The information provided in the paragraphs above are a brief summary of the "Treasury Management Monitor 2 Mid Year Review and Prudential Indicators 2011/12" report for scrutiny by Audit & Governance Committee Members.

Consultation

8. Not applicable

Options

9. It is a statutory requirement under Local Government Act 2003 for the council to operate in accordance with the CIPFA prudential Code and the CIPFA Treasury Management in the Public Services Code of Practice "the Code". The revised "code" was approved at full Council on 26 February 2010. The Council also approved the Treasury Management Strategy Statement and Prudential Indicators for 2010/11 to 2014/15 which stated that "The Treasury Management Reporting arrangements set out in paragraph 16, table 1, as described by "the Code" and the terms of reference in the Constitution be amended to include that Audit & Governance Committee scrutinise the Treasury Management Strategy and Monitoring reports." No alternative options are available.

Corporate Priorities

10. Treasury management is an integral part of the council's finances providing for cash flow management and financing of capital schemes. It aims to ensure that the council maximises its return on investments, (whilst the priority is for security of capital and liquidity of funds) and minimises the cost of its debts. This allows more resources to be freed up to invest in the Council's priorities, values and imperatives, as set out in the Corporate Strategy. It therefore underpins all of the council's aims.

Implications

11. The implications are
- Financial – the security of the Councils capital funds is a priority, maximising returns on investments is still key along with minimising the finance costs of debt.
 - Human Resources - there are no human resource implications to this report.
 - Equalities - there are no equality implications to this report.
 - Legal - there are no legal implications to this report.
 - Crime and Disorder - there are no crime and disorder implications to this report.
 - Information Technology - there are no information technology implications to this report.
 - Property –there are no property implications to this report.
 - Other - the revised code may have implications for the requirements placed on officers and members for the scrutiny and management of the treasury function.

Risk Management

12. The treasury management function is a high-risk area because of the volume and level of large money transactions. As a result of this the Local Government Act 2003 (as amended), the CIPFA Prudential Code and the CIPFA Treasury Management in the Public Services Code of Practice 2009 (the code) are all adhered to as required.

Recommendations

13. That Audit & Governance Committee note the Treasury Management Monitor 2 and Prudential Indicators 2011/12 at Appendix A.

Reason: That those responsible for scrutiny and governance arrangements are updated on a regular basis to ensure that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

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Report Date 05/12/1
approved 1

Specialist Implications Officer(s) None

Wards Affected: *List wards or tick box to indicate all* **All**

For further information please contact the author of this report

Background Working Papers

Local Government Act 2003 and amendments

CIPFA Prudential Code

CIPFA Treasury Management in the Public Services: Code of
Practice and Cross-Sectoral Guidance (“the Code”)

Treasury Management Strategy Statement and Prudential
Indicators for 2011/12 to 2015/16

Annexes

1. Appendix A - Treasury Management Monitor 2 Mid Year Review and Prudential Indicators 2011/12
2. Annex A – prudential Indicators 2011/12

PRUDENTIAL INDICATORS Monitor 2 2011/12 AND REVISED BUDGET HRA REFORM		2011/12 Original Budget	2011/12 Monitor 2	2011/12 REVISED BUDGET
1) Capital Expenditure To allow the authority to plan for capital financing as a result of the capital programme. To enable the monitoring of capital budgets to ensure they remain within budget	Non - HRA	£'000 51,478	£'000 61,415	£'000 61,415
	HRA	7,305	10,707	122,702
	TOTAL	58,783	72,122	184,122
2) Ratio of financing costs to net revenue stream This indicator estimates the cost of borrowing in relation to the net cost of Council services to be met from government grant and council taxpayers. In the case of the HRA the net revenue stream is the income from Rents and Subsidy	Non - HRA	9.59%	10.06%	10.06%
	HRA	2.06%	2.10%	2.10%
3) Incremental impact of capital investment decisions - Council Tax Shows the actual impact of capital investment decisions on council tax. The impact on council tax is a fundamental indicator of affordability for the Council to consider when setting forward plans. The figure relates to how much of the increase in council tax is used in financing the capital programme and any related revenue implications that flow from it.		£ p	£ p	£ p
	Increase in Council Tax (band D) per annum	22.85	24.09	24.09
4) Incremental impact of capital investment decisions - Hsg Rents Shows the actual impact of capital investment decisions on HRA rent. For CYC, the HRA planned capital spend is based on the government's approved borrowing limit so there is no impact on HRA rents.		£ p	£ p	£ p
	Increase in average housing rent per week	0.00	0.00	0.00
5) Capital Financing Requirement as at 31 March Indicates the Council's underlying need to borrow money for capital purposes. The majority of the capital programme is funded through government support, government grant or the use of capital receipts. The use of borrowing increases the CFR.	Non - HRA	160,738	162,023	162,023
	HRA	18,869	18,794	130,794
	TOTAL	179,607	180,817	292,817
6a) Authorised Limit for external debt - The authorised limit is a level set above the operational boundary in acceptance that the operational boundary may well be breached because of cash flows. It represents an absolute maximum level of debt that could be sustained for only a short period of time. The council sets an operational boundary for its total external debt, gross of investments, separately identifying borrowing from other long term liabilities for 3 financial years.	borrowing	212	212	337
	other long term liabilities	10	10	10
	TOTAL	222	222	347
6b) Operational Boundary for external debt - The operational boundary is a measure of the most likely, prudent, level of debt. It takes account of risk management and analysis to arrive at the maximum level of debt projected as part of this prudent assessment. It is a means by which the authority manages its external debt to ensure that it remains within the self imposed authority limit. It is a direct link between the Council's plans for capital expenditure; our estimates of the capital financing requirement; and estimated operational cash flow for the year.	borrowing	192	192	317
	other long term liabilities	10	10	10
	TOTAL	202	202	327
7) Adoption of the CIPFA Code of Practice for Treasury Management in Public Services Ensuring Treasury Management Practices remain in line with the SORP.	TM Policy Statement 12 TM Practices Policy Placed Before Council Annual Review Undertaken			
8a) Upper limit for fixed interest rate exposure The Council sets limits to its exposures to the effects of changes in interest rates for 3 years. The Council should not be overly exposed to fluctuations in interest rates which can have an adverse impact on the revenue budget if it is overly exposed to variable rate investments or debts	Net interest re fixed rate borrowing / investments Actual Net interest re fixed rate borrowing / investments	110%	110%	110%

8b)	<p>Upper limit for variable rate exposure</p> <p>The Council sets limits to its exposures to the effects of changes in interest rates for 3 years. The Council should not be overly exposed to fluctuations in interest rates which can have an adverse impact on the revenue budget if it is overly exposed to variable rate investments or debts</p>	<p>Net interest re variable rate borrowing / investments</p> <p>Actual Net interest re variable rate borrowing / investments</p>	-10%	-10%	-10%
9)	<p>Upper limit for total principal sums invested for over 364 days</p> <p>To minimise the impact of debt maturity on the cash flow of the Council. Over exposure to debt maturity in any one year could mean that the Council has insufficient liquidity to meet its repayment liabilities, and as a result could be exposed to risk of interest rate fluctuations in the future where loans are maturing. The Council therefore sets limits whereby long term loans mature in different periods thus spreading the risk.</p>		£10,000	£10,000	£10,000
10)	<p>Maturity structure of new fixed rate borrowing during 2010/11</p> <p>The Council sets an upper limit for each forward financial year period for the level of investments that mature in over 364 days. These limits reduce the liquidity and interest rate risk associated with investing for more than one year. The limits are set as a percentage of the average balances of the investment portfolio.</p>		Upper Limit	Mon 2	REVISED
		under 12 months	10%	6%	10%
		12 months and within 24 months	10%	2%	10%
		24 months and within 5 years	25%	6%	25%
		5 years and within 10 years	40%	23%	40%
		10 years and above	90%	63%	90%

Glossary Of Abbreviations

HRA Housing Revenue Account

CYC City of York Council

SORP Statement of Recommended Practice for Local Authorities

CFR Capital Financing Requirement

1. In accordance with the Prudential Code, the Prudential Indicators set by full Council on 24th February 2011 for the financial year 2011/12 must be monitored and reported through the financial year. The HRA reform and the requirement to borrow an additional £112m has changed key indicators which require Council approval. The Prudential Indicators are detailed above and some of the key points are explained below:
2. Size of the **Capital Programme (Indicator 1)** - The capital programme expenditure at monitor 2 is estimated at £72.122m the original budget was £73.024m. The Capital Programme Monitor 2 report provides further information with regards to the movements. The HRA Reform increase the HRA Capital Expenditure by £112m, therefore the total capital expenditure now stands at £184.122m
3. **Net revenue Stream (indicator 2)** - This indicator represents how much borrowing for the capital programme will cost as a percentage of the net revenue stream. The General Fund indicator at Monitor 2 is 10.06% compared to a budgeted level of 9.59%. The indicator has increased as the capital expenditure of the Council has increased and will be funded by borrowing. The Housing Revenue Account (HRA) indicator at monitor 2 is 2.10% compared to the budgeted level of 2.06%. The HRA reform

indicator is the same as at monitor 2 because the £112m capital expenditure is paid to the government on 28 March 2011 and for the year 2011/12 the HRA subsidy system remains in place. Therefore there is no change to the Net Revenue Stream.

4. **Incremental Impact on the Level of Council Tax (Indicator 3)** – This indicator shows the impact of capital investment decision on the bottom line level of Council Tax. The Council funds its discretionary capital programme from two main sources, from unsupported borrowing or using capital receipts from the sale of surplus assets. The Council's policy is to use capital receipts to fund the Capital programme, however in the current economic environment with reduced capital receipts there is the requirement to use unsupported borrowing, which has an impact on Council Tax. The unsupported borrowing is not taken unless it is affordable, sustainable and prudent and can be supported by an existing budget. At monitor 2 the impact on council tax is estimated at £24.09 per Band D charge. This has increased from the estimate of £22.85 due to the increase in borrowing required to support the capital programme, which is in line with indicator 2.
5. **Incremental Impact on the Level of Housing Rents (Indicator 4)** – The estimate in the original 2011/12 strategy, monitor 2 and the revised HRA reform indicator are all zero. This is because even though the level of this indicator changes, the level of housing rent is not affected as housing rent is set in accordance with government formula.
6. **Capital Financing Requirement (CFR) (Indicator 5)** - The CFR at Monitor 2 is estimated at £180.817m, which is the Council's underlying need to borrow for all capital investment over time. The CFR will fluctuate as new schemes are introduced into the capital programme and the funding position changes (as a result of external contributions, reductions in grants, changes to capital receipts etc) to support the Capital investment of the Council. The CFR under the HRA Reform has increased in line with the increased capital expenditure requirement of £112m. Therefore the revised CFR to incorporate the HRA reforms is £292.817m
7. **Authorised Limit / Operational Boundary (Indicator 6)** – The Council debt position at 1 April 2011 was £133.1m and currently stands at £135.1m. The Council's Operational Boundary (maximum prudent level of debt) was approved at Council as part of the budget set at £202m, along with the Authorised Limit (maximum allowed debt) at £222m. The headroom available within these limits allows the Council the ability to borrow in advance of need in accordance with its 3 year forecast Capital programme. If these limits were breached the LG Act 2003 requires full

Council approval. Under the HRA reform, the Authorised Limit will be breached with the capital expenditure payment of £112m. The Authorised Limit and Operational Boundary have increased accordingly to £347m and £327m respectively. Request for Council approval is recommended in the Treasury Management report.

8. **Adoption of the CIPFA Code of Practice in Treasury Management (Indicator 7)** – In accordance with the Prudential Code the Council has adopted the revised Treasury Management Code of Practice on 24 February 2011 and as detailed in the table has adhered to the requirements.
9. **Upper Limit for Fixed and Variable Interest rate Exposure (Indicator 8)** – Interest rate exposure on debt is positive due to it being in relation to interest paid on borrowing and on investments is negative as it is interest being received. When the variable and fixed interest rates are totalled, it will always be 100%. If the majority of the interest received by the Council is fixed and the interest paid on debt is fixed then the closer the actual fixed interest rate exposure will be to 100% and the variable rate exposure to zero. The limits set in the budget were not breached and at Monitor 3 fixed rate exposure was at 110% and variable rate exposure – 10%. The HRA reform does not affect this indicator
10. **Upper Limit for total principal sums invested for over 364 days (Indicator 9)** – This has been set at £10m and is approximately 17% of the total average investment portfolio. To date in 2010/11, no funds have been invested for longer than 364 days due to the uncertainty in the current economic environment and no value to be obtained from the longer rates available to the council within its credit criteria limits.
11. **Maturity structure of fixed rate borrowing in 2010/11 (Indicator 10)** – The borrowing portfolio is spread across different time periods to ensure that the Council is not exposed to the requirement to take new borrowing in any one year and be exposed to interest rates in any one year. Currently in 2010/11 the borrowing portfolio maturity profile is within the limits set. Under the HRA reform, further work is to be carried out with Housing Services to review the HRA business model and assess the optimal profile for when borrowing is to be taken. At this stage it is estimated that the current limits will allow for the requirements of the HRA reform borrowing maturity profile.

Cabinet

Report of the Cabinet Member for Corporate Services

Treasury Management Monitor 2 Mid Year Review and Prudential Indicators 2011/12

Summary

1. This Council is required through regulations issued under the Local Government Act 2003 and the revised 2009 (Chartered Institute of Public Finance and Accountancy) Code of Practice for Treasury Management to provide Members with an update on treasury management activities at least twice a year.
2. This report recommends changes to the 2011/12 Treasury Management Strategy Statement and Prudential Indicators in light of the HRA reform changes. It also updates on the Treasury Management activities for the period 1 April 2011 to 30 September 2011.
3. This mid year report highlights the economic environment for the first six months of the 2011/12 financial year and reviews the Council's Treasury Management activities covering:
 - Treasury Management Strategy Statement
 - HRA reform
 - Compliance with Prudential Indicators
 - Annual Investment Strategy
 - Investment portfolio
 - Borrowing portfolio

Background

4. The Council's Treasury Management function is responsible for the effective management of the Council's investments, cash flows, its banking, money market and capital transactions; the

effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.

Economic Background and Analysis

5. The Council's treasury management activities have operated within the following economic background over the last 6 months to 30 September 2011:
 - (a) Indicators suggest that the economy has at best stagnated;
 - (b) Conditions on the high street have deteriorated further;
 - (c) Employment has fallen again;
 - (d) The public finances are expected to miss this year's fiscal forecasts;
 - (e) CPI inflation rising, heading for a peak of around 5% in Q4;
 - (f) The MPC signal a move towards increasing QE further;
 - (g) Equities prices plummet and gilt yields fall to historic lows;
 - (h) The economic recoveries falter in the US and Europe
6. There remains huge uncertainties in economic forecasts due to:
 - (a) The decision by the MPC to expand quantitative easing over the next four months by a further £75bn which had an immediate effect of depressing gilt yields at the long end of the curve. This clearly underlines how concerned the MPC is about the prospects for growth of the UK economy and that recession is now a greater concern than inflation.
 - (b) The marked deterioration of growth prospects in the US, EU and UK, especially with increased concerns over Greece and the potential fall out from their debt situation. This has led in turn to a further increase in safe haven flows into UK gilts, which have depressed gilt yields and PWLB rates to lower levels.
7. From the economic uncertainty described above, it is expected that low growth in the UK will continue, with a low Bank rate for at least 24 months.
8. Figure 1 below shows the actual and projection of the bank base rate, which has remained at historically low levels since April 2009. The Council's treasury management advisers – Sector – forecast the position of the base rate in January 2011 for the 2011/12 Treasury Management Strategy this is compared to their revised forecast in August 2011. Other economists latest forecast are shown in May 2011. The graph highlights the delay in the

expectation of the increase in the Bank Base rate which is as a result of the decision to expand quantitative easing and deterioration of growth prospects.

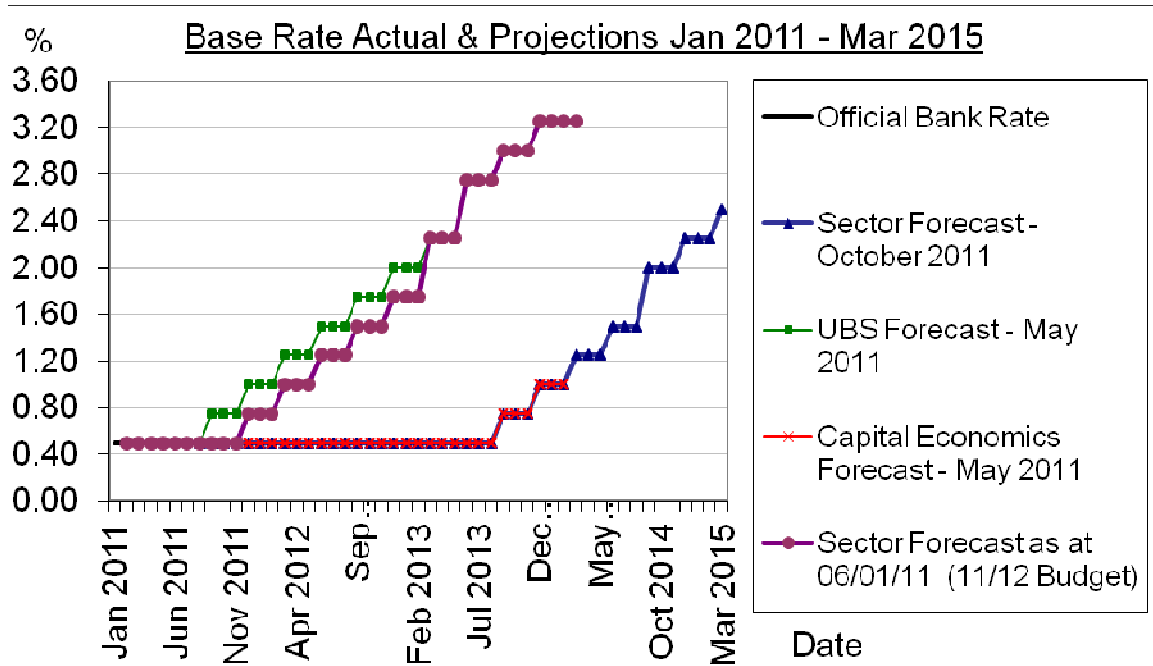


Figure 1: Base Rate 2011 to 2015 - latest forecast August 2011

Treasury Management Strategy Statement (TMSS)

9. The Treasury Management Strategy Statement (TMSS) for 2011/12 was approved by this Council on 24 February 2011. Included in the TMSS are Prudential Indicators which determine and keep under review how much the Council can afford to borrow. This is a statutory requirement under Section 3 of the Local Government Act 2003 and supporting regulations.
10. If these Prudential Indicators change along with the TMSS, it is a legal requirement to seek Council approval for these changes.
11. The TMSS approved previously, currently requires revision in light of the proposed changes to the current HRA subsidy arrangements. The following paragraphs explain the proposed HRA reform, the resultant required changes to the TMSS and prudential and treasury limits.

HRA Reform

12. The proposed reform of the HRA subsidy arrangements are expected to take place on 28 March 2012. This will involve the Council paying £112m to the Department of Communities and Local Government (CLG) which will remove the Council from the current HRA subsidy system. It should be noted that this figure will change slightly between now and the 28 March 2012 due to the impact of inflation.
13. This one off payment of £112m will ensure that the HRA will no longer make future annual payments to the CLG through the housing subsidy system. It is expected that the overall impact will be beneficial to the Council.
14. The HRA capital expenditure payment will be financed by a form of borrowing. This could be a money market loan or a bond but is more likely to be a Public Works Loan Board (PWLB) Loan as the Government announced on the 18th September that Local Authorities will be able to borrow from the PWLB at lower rates than currently offered by the PWLB. The level of rates will be approximately 0.15% above the level of the gilt, rather than the current PWLB rate of 1% above the gilt. These rates apply solely for the purpose to borrow for the HRA reform and are at the level which all PWLB rates were at prior to the Comprehensive Spending Review in October 2010. The HRA PWLB rates will be available from January 2012.
15. The legislative framework to enable the HRA reform to take place is yet to be agreed by Government in the White Paper in November 2011. The inclusion of the HRA reform in this treasury management report enables members to recommend to Council the approval for the change in the Prudential Indicators. This will allow the Council to borrow and take advantage of favourable PWLB rates when they become available in January 2012.
16. The original Prudential Indicators approved at Council on 24 February 2011 are attached at Annex A and are compared with the revised limits to incorporate the HRA reform requirement. Further explanation of the Prudential Indicators are detailed in the paragraphs below.
17. Further information on the HRA Reform will be reported to Members in the coming months, this will include further detail on

the required HRA borrowing portfolio in conjunction with housing services.

Compliance with Prudential Indicators

18. The Prudential Indicators included in the TMSS are based on the requirements of the Council's Capital programme. The Capital programme is an amount of capital expenditure which is funded from various external resources e.g. grants, revenue contributions etc and also borrowing. The level of borrowing required to support the capital programme over time is known as the Capital Financing Requirement.
19. The one off payment to the DCLG to remove the HRA from the current housing subsidy system is expected to be £112m. The £112m is capital expenditure which forms part of the capital programme and will increase the level of borrowing of the Council. The Council has to ensure that total capital investment (capital expenditure) remains within sustainable limits which are affordable and prudent.
20. It is a statutory duty for the Council to determine and keep under review the "Affordable Borrowing Limits". Council's approved Prudential Indicators (affordability limits) for 2011/12 are outlined in the approved Treasury Management Strategy Statement (TMSS) at Council on 24 February 2011. During the financial year to date the Council has operated within the Prudential Indicators set out in the Council's TMSS. The monitoring of the Prudential Indicators is attached at Annex A, along with the revised limits for the HRA reform. Prudential Indicators were not breached during the first 6 months of 2011/12.
21. Affordability - how much the council can afford to borrow – is determined by the "Authorised Borrowing Limit" and the "Operational Boundary". The "Authorised Limit" represents the legislative limit specified in the Act and the "operational boundary" is the maximum level of debt allowed for on going operational purposes. If the Authorised Borrowing limit is to be breached, a revised limit needs to be approved by full Council.
22. The key indicators which have changed in relation to the HRA reform are the Authorised Borrowing Limit which was £22m and

has been revised for approval to £347m, the Operational Boundary is now set at £327m, it was £202m and the Capital Financing Requirement has risen to £292.8m from £180.8m

23. Members are therefore requested to approve the changes to the Council's Prudential Indicators for 2011/12 shown in Annex A.

Annual Investment Strategy

24. Treasury Management Strategy Statement for 2011/12 was approved by Council on 24 February 2011. The Council's Annual Investment Strategy, which is incorporated in the Strategy, outlines the Council's investment priorities as follows:

- security of capital
- liquidity
- yield

25. The Council will aim to achieve the optimum return (yield) on investments commensurate with the proper levels of security and liquidity. Investments are placed with highly credit rated financial institutions using the creditworthiness matrices described in the Treasury Management Strategy, which includes sovereign credit ratings from the rating agencies and the credit default swap (CDS) overlay information provided by Sector.

26. The current economic climate with the continuing Euro zone sovereign debt crisis and its potential impact on banks prompts a low risk and short term strategy. It is considered appropriate to keep investments short with a maximum duration of 3 months. This applies to all entities in which the Council is considering investing, except for the following institutions:

- (a) UK Government and related entities such as Local Authorities – suggested limit remains at 5 years
- (b) UK semi-nationalised institutions e.g. Lloyds / RBS – suggested limit remains at 1 year. UK ownership provides considerable conform to investors.
- (c) Money market Funds – suggested limit remains at 1 year.

27. Investments held during the first six months of 2011/12, in accordance with Sector's Creditworthiness matrices and changes to Fitch and Moody's credit ratings, remained within the Council's approved credit criteria limits contained in the Annual Investment Strategy.

Investment Portfolio

28. Investment rates available in the market continue to remain at a historical low point. The average level of funds available for investment purposes in the six months of 2011/12 was £57.5m. The level of funds available is largely dependent on the timing of the Council's cash flow as a result of precept payments, receipt of grants, borrowing and progress on the Capital Programme. These funds are therefore available on a temporary basis dependant on cash flow movement.
29. The authority holds some core cash balances for investment purposes, i.e. funds available for a year or more, however to date in 2011/12 no funds have been invested for periods greater than one year due to the limited institutions available for investment in accordance with the credit criteria policy. This is a continuation of similar market conditions which prevailed through the majority of 2008/09 and through the whole of 2009/10 and 2010/11.
30. Treasury Management investment activity during the first six months of 2011/12 earned an interest rate of return of 1.5%. This is 1.03% better than the average 7 day London Inter-Bank Deposit rate (LIBID) of 0.47% and 1% higher than the average base rate for the period of 0.50%. The interest earned to date in 2011/12 is in line with the treasury management budget.
31. The higher rate of return on investment activity compared to the average LIBID rate and base rate for the period is due to the treasury team continuing to monitor the market and taking advantage of opportunities when they become available, whilst ensuring the security of the council's funds. Investments in the portfolio are diversified and include deposits of short term call accounts, fixed term and money market funds.
32. Figure 2 shows the interest rates available on the market between 7 days and 1 year and also the rate of return that the Council has achieved for the first six months of 2011/12. It shows that favourable / competitive interest rates have been obtained for investments whilst ensuring the required liquidity and security of funds for the Council.

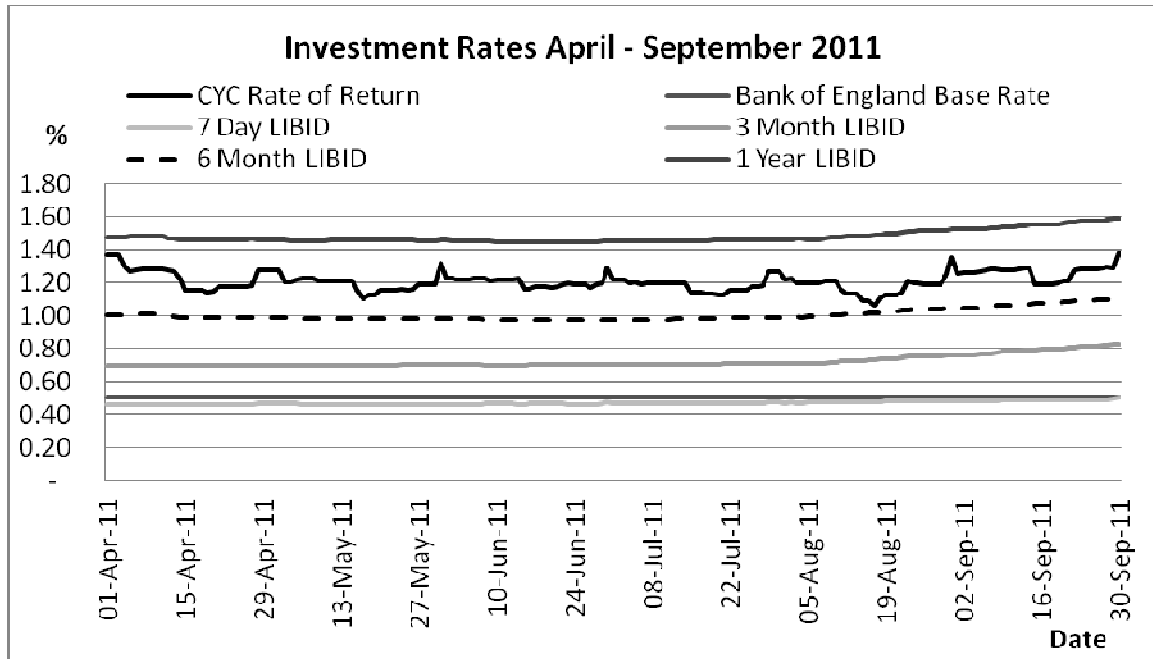


Figure 2 CYC Investments vs Money

Market Rates

Borrowing Portfolio

33. The Council undertakes long term borrowing in accordance with the investment requirements of the capital programme and all borrowing is therefore secured against its asset base.
34. The level of borrowing taken by the Council is determined by the Capital Finance Requirement (the Councils underlying need to borrow for capital expenditure purposes). Borrowing needs to be affordable, sustainable and prudent and the treasury management budget supports the borrowing finance costs in the longer term.
35. Under regulation, the Council can borrow in advance of need in line with its future borrowing requirements in accordance with the Capital Financing Requirement. The Administrative Accommodation project increases the Council's need to borrow over the next year and therefore the markets will continue to be closely monitored to ensure that advantage is taken of favourable rates in 2011/12 and the increased borrowing requirement is not as dependant on interest rates in any one year.
36. On the reverse side, the Council's level of borrowing can also be below the Capital Financing Requirement. This would mean that instead of increasing the Council's level of borrowing, surplus

funds held for investment purposes would be utilised instead, decreasing the level of surplus funds being available for investment. In the current interest rate environment where investment rates are below borrowing rates consideration is given to the value of taking borrowing or whether it is better for the council to keep investment balances lower.

37. Sector - treasury management advisers - forecast that future PWLB rates will also rise. The market is expected to remain volatile over the coming months but from 2012 rates are expected to be on a rising trend. Therefore, rates are being monitored to take advantage of long term low attractive borrowing rates, whilst being mindful that investment rates are to remain low for the foreseeable future.
38. The Councils long-term borrowing started the year at a level of £133.1m. A £5m loan was repaid in May 2011 in line with its maturity date. New borrowing of £7m was taken in August 2011.
39. The loans taken in 2011/12 are below the original target of 5% set in the Council approved 2011/12 strategy, the £5m 10 year loan was at 3.81% and the £2m 5 year loan at 2.54%. At this Treasury Management Monitor 2 report the target level for loans for the remainder of 2011/12 is 4.3%.
40. Figure 3 shows the fluctuation in PWLB rates since October 2010 when the Comprehensive Spending Review increased rates to 1% above gilt yields. It highlights when the new borrowing in 2011/12 has taken place, compared to rates available.

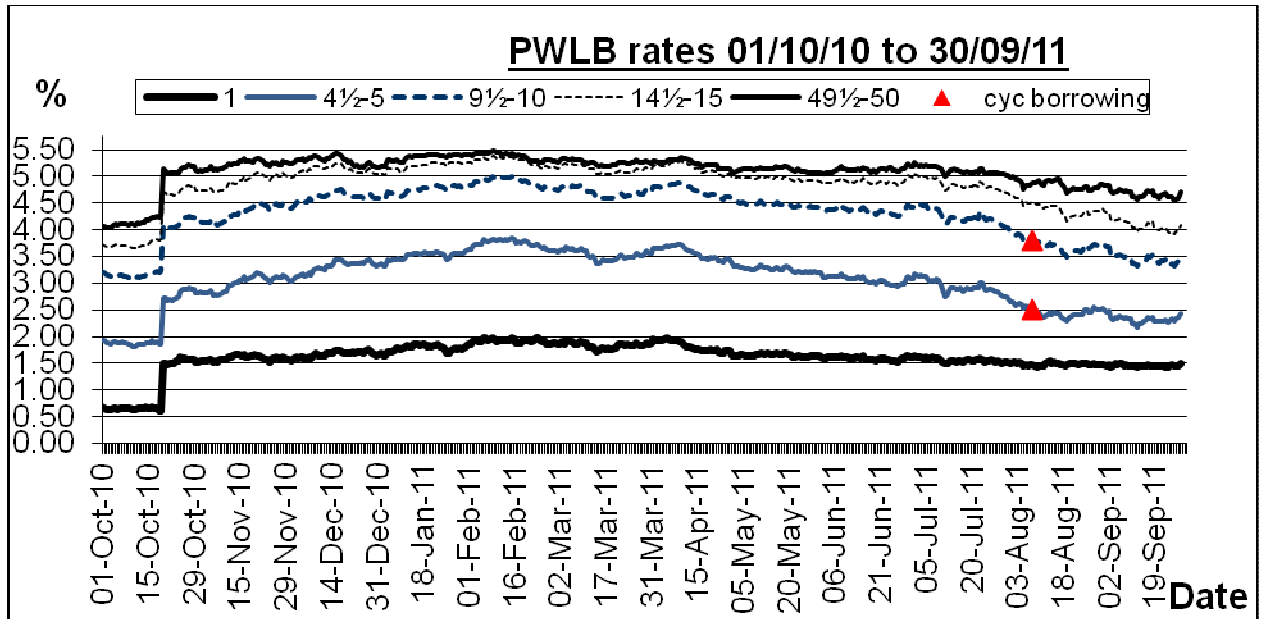


Figure 3 – PWLB rates vs CYC Borrowing Levels

41. Figure 4 illustrates the 2011/12 maturity profile of the Council’s debt portfolio updated to reflect the borrowing this year to 30 September 2011. The maturity profile shows that there is no large concentration of loan maturity, thereby spreading the interest rate risk dependency in any one year.

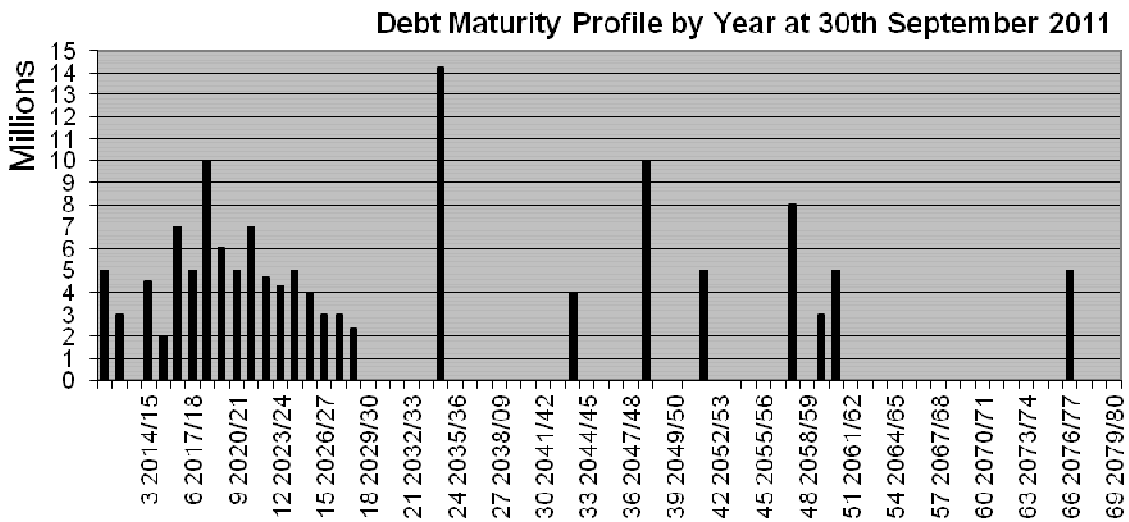


Figure 4 – Debt Maturity Profile 11/12

Consultation

42. The report shows the position of the treasury management portfolio in 2011/12 and provides initial information regarding the future HRA reforms. A further report will be provided to Members

on the HRA reforms in the coming months. The treasury management budget was set in light of the council's expenditure plans and the wider economic market conditions, based on advice from Sector - the Council's Treasury Management advisors.

Corporate Priorities

43. The Council's corporate strategy has the priority to ensure value for money and efficiency of its services. Treasury Management aims to achieve the optimum return on investments commensurate with the proper levels of security, and endeavours to minimise the interest payable by the Council on its debt structure.

Human Resources Implications

44. There are no HR implications as a result of this report.

Equalities

45. There are no equalities implications as a result of this report.

Legal Implications

46. Treasury Management activities have to conform to the Local Government Act 2003, the Local Authorities (Capital; Finance and Accounting) (England) Regulations 2003 (SI 2003/3146), which specifies that the Council is required to have regard to the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice and also the *Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008* (SI 2008/414), which clarifies the requirements of the Minimum Revenue Provision guidance.

Crime and Disorder Implications

47. There are no crime and disorder implications as a result of this report.

Information Technology Implications

48. There are no IT implications as a result of this report.

Property Implications

49. There are no property implications as a result of this report.

Risk Management

50. The Treasury Management function is a high-risk area because of the level of large money transactions that take place. As a result of this there are procedures set out for day to day treasury management operations that aim to reduce the risk associated with high volume high value transactions. These are detailed in the Treasury Management strategy Statement at the start of each financial year.

Recommendations

51. Members are requested to recommend to full Council to:
- Approve the changes to the Prudential Indicators in light of the HRA reform, specifically the Authorised Borrowing Limit at £347m
 - Note the HRA reform is to be approved by the Government White paper in November 2011 and payment of £112m to the CLG on 28 March 2011
 - Note the expected impact on the capital and treasury activities of the HRA reform
 - Note the Treasury Management activities in 2011/12

Reason – to ensure the continued performance of the Council's Treasury Management function and the inclusion of the affects of the HRA reform on treasury management activities.

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Report Date 1/11/11
Approved

Wards Affected:

All

Specialist Implication Officers:

None

For further information please contact the author of the report

Background Papers

Cash-flow Model 11/12, Investment Register 11/12, PWLB Debt Register, Capital Financing Requirement 11/12, Venture Fund 11/12, Treasury Management budget 11/12, Statistics 11/12.

Annexes

Annex A – Prudential Indicators 2011/12

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