AUDIT COMMITTEE AGENDA

HARTLEPOOL BOROUGH COUNCIL

Friday, 3 December 2010

at 9.00 am

in Committee Room A, Civic Centre, Hartlepool

MEMBERS: AUDIT COMMITTEE:

Councillors C Akers-Belcher, H all, Hill, J W Marshall, Preece, Turner and Wells.

1. **APOLOGIES FOR ABSENCE**

2. **TO RECEIVE ANY DECLARATIONS OF INTEREST BY MEMBERS**

3. **MINUTES**

3.1 To confirm the minutes of the meeting held on 22 September 2010

4. **ITEMS FOR DISCUSSION/DECISION**

4.1 Treasury Management Strategy Update 2010/2011- *Chief Finance Officer*
4.2 Audit Commission Report- Annual Audit Letter – *Chief Finance Officer*
4.3 Internal Audit Plan 2010/11 Update – *Head of Audit and Governance*
4.4 Internal Audit Charter – *Head of Audit and Governance*
4.5 Internal Audit Strategy – *Head of Audit and Governance*
4.6 Role Of Audit Committee In Approving Audit Plans – *Head of Audit and Governance*
4.7 Treasury Management 2011/2012 – *Chief Finance Officer*
4.8 International Financial Reporting Standards (IFRS) –Update – *Chief Finance Officer*

5. **ANY OTHER ITEMS WHICH THE CHAIR CONSIDERS ARE URGENT**

AUDIT COMMITTEE

MINUTES AND DECISION RECORD

22 September 2010

The meeting commenced at 9.00 am in the Civic Centre, Hartlepool

Present:

Councillor: Christopher Akers-Belcher (In the Chair)

Councillors: Gerard Hall, Arthur Preece and Ray Wells

In accordance with Council Procedure Rule 4.2 Councillor Ann Marshall was also present as substitute for Councillor John W Marshall

Officers: Chris Little, Chief Finance Officer
Noel Adamson, Head of Audit and Governance
Sandra Shears, Chief Accountant
Jo Wilson, Democratic Services Officer

Audit Commission Representatives:
Diane Harold, Lynn Snowball and Sue Reeve

13. Apologies for Absence

Apologies were submitted by Councillor J W Marshall.

14. Declarations of interest by Members

None

15. Confirmation of the minutes of the meeting held on 25 August 2010

Confirmed.

The Chair queried whether Members' comments on counter-fraud initiatives had been fed into the budget process. The Chief Finance Officer indicated that this would be done at the appropriate stage of proceedings.

16. Internal Audit Plan 2010/11 Update (*Head of Audit and Governance)*

Purpose of report

To inform members of the progress made to date completing the internal audit plan for 2010/11.

Issue(s) for consideration by the Committee

Appendix A to the report detailed the pieces of work that had been completed while Appendix B detailed the audits ongoing at the time the report was compiled. The Head of Audit and Governance highlighted the recommendations which had been made regarding primary schools, commenting that this was not a reflection on the schools themselves however financial standards were becoming increasingly difficult to attain and schools had limited administrative resources available to them. Members were also advised that Contact Point had recently been scrapped, however as the audit had been conducted prior to this announcement the details were included within the report.

Internal Audit Team had also been involved with the following working groups:

Information Governance Group
Procurement Working Group
Performance and Risk Management Group

The Team was in the process of ensuring arrangements were in place to provide the required data matches to the Audit Commission in relation to the National Fraud Initiative for 2010/11. The work completed and ongoing was in line with expectations at this time of the year.

A Member queried the minimum criteria for passwords for the Careworks system. The Head of Audit and Governance confirmed that this was a national database and the set up of passwords was dictated by the software itself. The Chief Finance Officer commented that Hartlepool Council currently had a two-tier security arrangement for passwords to enable access to pc's which restricted access to all systems and therefore provided a higher level of security.

Decision

The report was noted.

17. Approval of 2009/2010 Statement of Accounts *(Chief Finance Officer)*

Purpose of report

To present the Audit Commissioner's Annual Governance Report and enable Members to approve the final 2009/2010 Statement of Accounts.

Issue(s) for consideration by the Committee

The Chief Finance Officer presented the report which included the Audit Commission's Annual Governance Report and enabled Members to approval the final 2009/10 Statement of Accounts.

During the audit a number of issues were identified by the Auditor and the Accounts were amended to reflect the issues detailed in Appendix 2, with the exception of item (ii), Change to Building Schools for the Future Reserve, these changes did not impact on the Council's Earmarked Reserves or General Fund Balances. The Chief Finance Officer commented that the closure of accounts had been particularly challenging this year owing to the implementation of the new staffing structure with key experienced staff leaving the authority. The Chief Financial Officer indicated that a late amendment to depreciation charges for infrasture assets had been agreed with the Auditors and a revised set of accounts were circulated. These changes did not impact on the Council's Earmarked Reserves of General Fund Balances.

The Chief Finance Officer also highlighted that a number of cross referencing adjustments made to the Accounts.

Members acknowledged what a challenging time this had been for the department dealing with a major reorganisation at the same time but noted that very constructive discussions had taken place on what could be learnt from the process undertaken this year to ensure a more streamlined process is in place. Overall the accounts provided positive messages on the continuing development of the management framework including the future challenges in delivery efficiencies through Business Transformation.

In response to a Member's question, the Chief Finance Officer explained the cash flow statement and commented that there were a few technical issues with the software package used but it was hoped that these would be rectified in the near future. The Chief Finance Officer advised Members that the key control for managing cash is the bank reconciliation, which is completed on a dialy basis as part of overall Treasury Management controls.

A discussion ensued on the Council's procurement process and what could be undertaken to further encourage local companies and suppliers to submit quotations to undertaken work or provide supplies to the Council. It was noted that Contract Scrutiny Committee were currently considering increasing the threshold contained within the Contract Procedure Rules as this should hopefully encourage more local companies to submit quotations.

The Chairman asked that the gratitude of the Committee be forwarded to everyone involved in the processing of the accounts in what had been very difficult circumstances.

Decision

(i) The matters raised in the Audit Commission's Annual Governance Report detailed in Appendix A were approved.
(ii) The reasons detailed in Appendix B to this document for not amending the Statement of Accounts to reflect the unadjusted mis-statements in the accounts were approved.
(iii) It was noted that the Chairman will sign the Letter of Representation detailed at Appendix 4 of the Annual Governance Report.
(iv) The Chief Finance Officer was instructed to implement the action plan detailed at Appendix 6 of the Annual Governance Report.
(v) The Final 2009/10 Statement of Accounts was approved.

18. Treasury Management Outturn 2009/2010 *(Chief Finance Officer)*

Purpose of report

To provide a review of Treasury Management activity for 2009/2010 and the outturn Prudential Indicators for this period.

Issue(s) for consideration by the Committee

The Chief Finance Officer presented the report which included a summary of the following key issues for the financial year 2009/10:

- The economic background for the year;
- The Council's capital expenditure and financing in 2009/10;
- The Council's overall treasury position, including borrowing and investment activity;
- The regulatory framework, risk and performance considerations, including compliance with key prudential indicators;
- Pooled Investment Fund termination.

As Members were aware, a training session for the Audit Committee on Treasury Management issues had been scheduled for Friday 8 October 2010 to enable Members to scrutinise Treasury Management issues more effectively in future years.

Decision

The report was noted.

19. Any other items which the Chair considers are urgent – Update on Audit Commission

A representative from the Audit Commission was in attendance and provided members with an update on the Audit Commission and the recent Government proposal to disband the Commission. Should this be agreed, the main difference would allow local organisations to appoint their own auditors. It had been suggested that regional co-operative groups would be created to maintain the current level of service provision.

The Chief Finance Officer questioned how auditors would be appointed. The representative from the Audit Commission commented that local authority audits may not be as lucrative to private sector auditors. It was noted that NHS Foundation Trusts currently appoint auditors and it may be worth ascertaining the processes they use.

It was suggested by a Member that if considering private auditors, the track record and history of that company should also be taken into account.

Decision

The update was noted.

The meeting concluded at 10.35 am.

CHAIR

AUDIT COMMITTEE

3 December, 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Chief Finance Officer

Subject: TREASURY MANAGEMENT STRATEGY UPDATE 2010/2011

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1. PURPOSE OF REPORT

1.1 To update the Members on matters relating to Treasury Management and to enable Members to confirm the continuation of the existing Treasury Management Strategy.

2. BACKGROUND

2.1 This report is presented to this committee in its role in reviewing Treasury Management activities.

2.2 The current Investment and Borrowing Strategy was approved by the Council on 29th January, 2010.

2.3 The CIPFA Code of Practice for Treasury Management recommends as best practice, interim reporting of Treasury Management activities. This report provides details of Treasury Management activity for the year to date. The review covers the following areas:

- Interest Rates and Economic Outlook
- Borrowing Strategy
- Investment Strategy and Counter Party Risk
- Prudential Code Monitoring and revisions to Prudential Limits

3. INTEREST RATES AND ECONOMIC OUTLOOK

3.1 UK short-term interest rates fluctuated in a very narrow range in the first half of the financial year. The Bank Rate was held at its record low of 0.5% in spite of above target inflation and evidence of a recovery in activity in most industrialised economies. The tenuous nature of the economic upturn, confidence that price pressures will abate and the still fragile state of the financial sector supported the case for the maintenance of an accommodative monetary policy.

3.2 Long-term interest rates peaked in the early stages of the financial year. The rise was reversed in May. The financial markets' confidence in the Coalition Government's Spending Review and deficit reduction plan encouraged new investment in gilt-edged securities. More important, however, was the financial crisis in the euro-zone, triggered by the threat of a sovereign debt default by Greece. This, together with evidence of decelerating growth in the US, ensured continued demand for high quality government debt and prior to the spending review, gilt yields and PWLB rates subsided towards their 2009 lows as a result.

3.3 Following the Chancellor's announcement of the Spending Review on 20th October, 2010, HM Treasury instructed PWLB to:

i) Increase the interest rate on all <u>new</u> loans to 1% above the Government's cost of borrowing. This change took immediate effect;
ii) Publish at the end of each month a list of individual loans it has made to local authorities, including the type, amount, term and rate applying to each loan.

3.4 HM Treasury has indicated "that the interest rates increase is based on the Government having to make difficult choices around borrowing and capital investment. To ensure that the rate at which loans are made available to local authorities better reflects the availability of capital funding post-spending review and encourages optional borrowing and investment decisions". Interestingly, the increase in PWLB rates will generate a surplus to the Treasury.

3.5 Local authorities will still be able to finance capital expenditure requirements by borrowing monies from banks. However, commercial banks will use PWLB interest rates as a benchmark and increase interest rates accordingly. The increase in PWLB interest rates therefore increases borrowing costs for local authorities at a time of reducing revenue grant funding. In the short term this is manageable owing to short term interest rates. However, in the medium term this change increases risk to the Council and this position will need to be managed carefully to protect the Council's longer term financial position.

3.6 HM Treasury have also indicated that publishing details of new PWLB loans is designed to increase transparency of decisions made by local authorities. In my view this is simply another layer of bureaucracy as the prudential code and associated reporting requirements already provide comprehensive arrangements for reporting on Treasury Management issues.

3.7 The underlying investment environment remains difficult for the Council, foremost being the improving, but still challenging, concerns over investment counterparty risk.

3.8 The table below details the forecast provided by Butlers for short term and long term borrowing rates.

Medium-Term Rate Estimates

Annual Average %	Bank Rate	Money Rates		PWLB Borrowing Rates		
		3 month	1 year	5 year	20 year	50 year
2009/10	0.5	0.7	1.3	3.0	4.4	4.5
2010/11	0.5	0.7	1.5	2.4	4.2	4.3
2011/12	1.1	1.3	2.2	3.1	4.8	4.9
2012/13	2.3	2.5	3.3	4.0	5.0	5.1
2013/14	3.3	3.5	4.0	4.5	5.0	5.0

3.9 As a result of the economic conditions described above, the Council continues to receive historically low investment returns in the medium term. This is now having a greater impact on the Council's finances as fixed deposits taken out before the drastic reduction to interest rates mature.

4. BORROWING STRATEGY

4.1 The Council's borrowing and investment position as at 9th November, 2010, was as follows:

	£m	Average Rate
Temporary Loans*	4.0	0.5%
PWLB Loans	1.8	6.9%
LOBO Loans	45.0	4.0%
Gross Debt	**50.8**	
Investments*	27.4	1.2%
Net Debt	**23.4**	

*Note that amounts shown only include the Council's share of investments held as part of the 'Pooled Investment Fund' and excludes the £10.9m held on behalf of the Cleveland Fire Authority.

4.2 The Council is currently under-borrowed in relation to its Capital Finance Requirement (CFR) which was £86.0m as at 31st March, 2010. This has been achieved by internalising the Council's borrowings and temporarily using reserves to avoid external borrowing. This has mitigated some of the counterparty risk that has been endemic in the financial markets in the first half year.

4.3 Long-term fixed interest rates are currently low but expected to rise over the three year planning period. The Bank Rate is expected to remain at 0.5% until mid 2011, before rising gradually. With rates at their current levels it continues to be advantageous to use the Council's own cash balances to temporarily fund its capital borrowing requirement. This strategy will avoid increasing cash holding at a time when counterparty risk remains high and investment returns are low. Therefore borrowing should be postponed until cash flow need is more apparent. Any temporary borrowing required will be with short term loans.

4.4 There may be a need to undertake some new long term borrowing if long term rates begin to rise in order to protect the Councils position in the future. This is because of the need to balance the risk of higher long term borrowing costs compared to minimising short term interest payments. Currently this is best achieved by the netting down of borrowing and investments, but this could change if long term interest rates begin to rise. The balance of the risks will be kept under review and the Chief Finance Officer will consider the most appropriate form of borrowing after taking into account the interest rates available at the time.

5. INVESTMENT STRATEGY AND COUNTER PARTY RISK

5.1 The level of investments as at 9th November, 2010, was £27.4m.

5.2 The Council's investment strategy is safeguarding the repayment of the principal and interest on its investments on time – the investment return being a secondary objective. Against the economic background described earlier the current investment climate has one overriding risk consideration, which is counterparty risk. As a result of this underlying concern the Chief Finance Officer is continuing the operational investment strategy which has tightened the controls that were already in place.

5.3 The original investments strategy included the approval of various criteria for determining the counterparties which the Council will invest funds with. In accordance with best practice the Council does not rely solely on credit agency ratings. Credit ratings have a role in determining the original list but are supplemented with additional considerations such as Government support.

5.4 The original criteria approved by Members provides a starting point which is then restricted further to produce an operational list which is reviewed on a regular basis. Following the increased risk and uncertainty arising from the unprecedented recent economic crisis the Chief Finance Officer has continued to adopt an even more vigilant approach resulting in what is effectively a 'named' list. This consists of a very select number of counterparties that are considered to be the lowest risk. This has involved the Council temporarily suspending making new deposits with all building societies except the Nationwide, which has a financial standing rating equivalent to the major clearing banks.

5.5 The Council's approach of suspending building societies from the counterparty list has proven prudent as the ratings for all building societies (except Nationwide) have recently been downgraded owing to continuing concerns about their financial stability and exposure to property loans.

5.6 The Council has also continued to exclude all foreign banks, including Irish banks from the list following the downgrading of the countries sovereign rating.

5.7 At the time of writing this report there was ongoing speculation about the solvency of Ireland and whether a European Union bail-out would be necessary. This position could potentially affect other European countries and in particular the so called "PIGS" countries (Portugal, Italy, Greece & Spain). It also continues to undermine confidence in Irish banks.

5.8 The counterparty list now includes organisations meeting the following more stringent criteria:

- The original 8 eligible institutions included within the Governments guarantee scheme. This includes the major clearing banks and the Nationwide.
- Banks with a AA rating
- The Government's Debt Management Office
- Other Local Authorities
- The Council's own Bank, the Co-Op

5.9 By not relying on credit ratings the Council is seeking to take a more pragmatic and broad based view of the factors that impact on counterparty risk. The downside of this prudent approach is a lower investment return than would be possible if deals were placed with organisations with a lesser financial standing.

5.10 As part of the approach to maximising security the Council has also kept investment periods short. This has also resulted in lower investment returns.

6. PRUDENTIAL CODE MONITORING

6.1 As part of the Treasury Strategy for 2010/2011 the Council set a number of prudential indicators. Compliance against theses indicators is monitored on a regular basis and there are no breaches of these limits to report.

6.2 The tables below show the revised Capital Financing Requirement and Capital Expenditure Funded by Borrowing estimates for 31 March

2011 and an explanation as to why these Prudential Indicators have changed:

Prudential Indicator	**31 Mar 2011 Original Estimate £000**	**31 Mar 2011 Revised Estimate £000**
Capital Financing Requirement (CFR)	101,960	95,347
The CFR has been revised to take into account the actual CFR as at 31 March 2010 and to reflect the decision to delete the £3m provision for the replacement of Mill House. The CFR has also been amended as a result of rephased capital expenditure from 2009/2010, expenditure in 2010/2011 that is anticipated to be rephased into 2011/2012 and a corresponding amendment to the Minimum Revenue Provision.		

Prudential Indicator	**31 Mar 2011 Original Estimate £000**	**31 Mar 2011 Revised Estimate £000**
Capital Expenditure Financed by Borrowing	13,608	13,459
Capital Expenditure Financed by Borrowing has been revised to reflect rephased capital expenditure from 2009/2010 and expenditure in 2010/2011 that is anticipated to be rephased into 2011/2012.		

7. CONCLUSIONS

7.1 The Council is currently funding some of its Capital Financing Requirement by using temporary cash balances. This is currently the most cost effective way to finance this expenditure in the short term and is minimising the Councils exposure to counterparty risks. When these resources are no longer available, the Council will use temporary borrowing until long term rates become more cost effective again.

8. RECOMMENDATION

8.1 For Members to note the report and the continuation of the Treasury Management Strategy.

AUDIT COMMITTEE

3 December 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Chief Finance Officer

Subject: AUDIT COMMISSION REPORT- ANNUAL AUDIT LETTER.

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1. PURPOSE OF REPORT

1.1 To inform Members of the Audit Committee that arrangements have been made for a representative from the Audit Commission to be in attendance at this meeting, to present the content of the Audit Commissions Annual Audit Letter.

2. BACKGROUND

2.1 This report summarises the findings from the 2009/10 audit. It includes messages arising from the audit of financial statements and the results of the work undertaken to assess arrangements to secure value for money in the use of resources.

3. FINDINGS OF THE AUDIT COMMISSION

3.1 Details of key messages from the work carried out are included in the main body of the report attached as **Appendix 1**.

4. RECOMMENDATIONS

4.1 That the Audit Committee:

i. note the report of the Audit Commission

Annual Audit Letter

Hartlepool Borough Council

Audit 2009/10

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

Contents

Key messages

This report summarises my findings from the 2009/10 audit. My audit comprises two elements: the audit of the Council's financial statements (pages 4 to 5) and my assessment of the Council's arrangements to achieve value for money in your use of resources (pages 6 to 9).

Audit opinion and financial statements

1 I issued an unqualified opinion on the Council's financial statements on 24 September 2010. My audit identified material errors that were corrected by the Council.

Value for money conclusion

2 I assessed your arrangements to secure economy, efficiency and effectiveness in the use of resources according to the criteria specified by the Audit Commission. I issued an unqualified opinion on your arrangements on 24 September 2010.

Current and future challenges

3 The Council has had to respond rapidly to cuts in capital and revenue funding for 2010/11and beyond. For example, the Council will now receive only £12.4 million of the expected £95 million funding from the Building Schools for the Future programme, and revenue grants to the Council were reduced by £2.2 million in 2010/11.

4 Local government is facing major operational and financial challenges. The Treasury announced £6.2 billion of in-year savings from government spending on 24 May 2010. Following the October spending review it has announced more significant cuts in funding over the next four years. The Government has also set out its ambition to promote the radical devolution of power and greater financial autonomy to local government and community groups, including a review of local government finance.

5 In response to the funding cuts and changes, the Council has continued to review its medium term financial plan. It has already begun analysing options so that it can quickly respond to the predicted cuts, including modelling on different levels and timings when funding reductions might happen ahead of the recent October spending review.

6 Robust financial management will be increasingly important to maintain a stable financial position and the Council's improvements in financial management in recent years will support this. The Council needs to review its services, approach to delivery and priorities in order to manage within reduced funding. The Council's Business Transformation Programme, with its Service Delivery Options will provide the organisational framework to help review services and manage this challenging task.

7 In addition, the Local Government Boundary Commission has carried out an electoral review of the Council. It has approved a new Council size of 33 members instead of the current 47 and is now consulting on ward boundaries. Having reduced its management capacity in the recent restructure, the Council will need to review the impact of these reductions. Members and officers will need to ensure there is a streamlined, robust and well focused governance framework and approach. This will help the Council meet the significant challenges it faces, with some potentially very difficult decisions to make.

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

8 I gave an unqualified opinion on the Council's 2009/10 financial statements on 24 September 2010, within the statutory target date.

9 There were several material errors and some minor errors. Disclosures and other notes were changed or developed.

10 Errors identified included:

- infrastructure assets in the Balance Sheet had not been depreciated over a number of years and the overall value was now materially overstated;
- categories of fixed assets had been misclassified;
- errors in financial instrument disclosures in the notes to the accounts; and
- cash flow statement errors.

11 There was a resulting net decrease in General Fund balances and Earmarked Reserves of £61,000. This partly related to a cut in government grants for 2009/10 announced by the Government in June 2010.

12 There were several added disclosures required after preparation of the draft financial statements. These were to address the cut in Local Public Service Agreement grant in 2009/10 as well as the abolition of the Building Schools for the Future Programme.

13 A post balance sheet event disclosure was also added following the announcement that increases in pensions would be linked to the Consumer Prices Index (CPI) instead of the Retail Price Index (RPI). The impact of this was estimated to have reduced the pension liability by £17.753 million.

14 Whilst the finance team faced particular challenges this year following a significant internal restructure of the central and departmental Finance teams, the financial statements contained more errors this year. I have recommended a number of actions to improve arrangements in my Annual Governance Report to the Audit Committee:

- ensure there is enough capacity and a detailed project plan to produce the financial statements under International Financial Reporting Standards in 2010/11, which will require additional time to complete;
- develop capital accounting capacity and technical knowledge in this area; and
- develop the Quality Assurance process of the unaudited and final revised financial statements to identify and correct errors and inconsistencies ahead of the audit.

International Financial Reporting Standards

15 The Council is making good progress in implementing the financial reporting changes required by introducing International Financial Reporting Standards (IFRS). These changes will be implemented for the 2010/11 statement of accounts with the 2009/10 accounts restated for the changes. The key changes are:

- revaluing and reclassifying property, land and buildings;
- recategorising lease agreements; and
- gathering information to support accruals for staff holidays not taken by the end of the year.

16 I will audit the restated 2009/10 accounts once they are available.

Internal control

17 I did not identify any significant weaknesses in the Council's internal control arrangements.

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 (VFM) conclusion.

2009/10 use of resources assessments

18 At the end of May 2010, the Audit Commission wrote to all chief executives to inform them that following the Government's announcement, work on CAA would cease with immediate effect and the Commission would no longer issue scores for its use of resources assessments.

19 However, I am still required by the Code of Audit Practice to issue a value for money conclusion. I have therefore used the results of the work completed on the use of resources assessment up to the end of May to inform my 2009/10 conclusion.

20 I have reported the significant findings from the work I have carried out to support the VFM conclusion.

Value for money conclusion

21 I issued an unqualified conclusion stating the Council had satisfactory arrangements to secure economy, efficiency and effectiveness in its use of resources.

22 I assessed the Council's arrangements to achieve economy, efficiency and effectiveness in its use of money, time and people against criteria specified by the Audit Commission. The Audit Commission specifies each year, which Key Lines of Enquiry (KLOE) are the relevant criteria for the VFM conclusion at each type of audited body, and these are detailed overleaf.

Criteria	Adequate arrangements?
Managing finances	
Planning for financial health	Yes
Understanding costs and achieving efficiencies	Yes
Financial Reporting	Yes
Governing the business	
Commissioning and procurement	Yes
Use of information	Yes
Good governance	Yes
Risk management and internal control	Yes
Managing resources	
Strategic asset management	Yes
Workforce	Yes

23 The Council has continued to develop and improve its arrangements to respond to the changing nature and role of local government. The Council has a good track record of managing organisational change successfully. It has streamlined its organisational structure, improving its focus and is delivering savings. The Council is rationalising and managing its estate to meet future requirements with sales of surplus property providing opportunities for ongoing savings. It still needs to develop asset management benchmarking and performance indicators to support improved management and value for money.

24 The Council's workforce is productive and skilled and clear about its responsibilities for improving the way it delivers services to the community. The Council works well with partners to ensure there is a shared focus on local priorities through, for example, joint workforce planning, which helps to avoid duplication. These all contribute to improving value for money.

25 The Council has well focused plans to make significant savings and improve value for money and it is on track to achieve these plans. The Council has an ambitious but realistic improvement programme, the Business Transformation Programme. This programme is fundamentally reviewing all council services, how they are provided and the resources needed to deliver them.

26 The Council has a good understanding of its costs and is improving this as it progresses through the Transformation Programme. It already has a good understanding of how to invest to maximise savings and benefits to users. This has enabled them to improve services and deliver high quality services in a challenging context. It is now helping it to decide how to deliver cost-effective services in future.

27 Financial management in the Council has improved. The Council is clearly linking priorities to service and financial planning and delivering efficiencies. Forecasting has improved and the Council has a good track record of delivering within budget.

28 The Council has realigned staffing capacity to deliver improvements through procurement. This will support the Council in its reviews of service delivery options as part of the Transformation Programme. Effective procurement is a key factor that will determine the savings it can achieve and the impact of any changes on services and the local community. The Council delivered savings of £300,000 through procurement in 2009/10 and has made procurement more open and transparent. Good examples of improvements and savings through effective procurement exist, but there is more work to be done to ensure that progress is made across all of the Council.

29 In-year reporting and monitoring arrangements have improved although year-end financial reporting in the financial statements still needs to improve. The Council now reports financial and performance information together, and more quickly than previously. High-spending and high-risk areas of work in particular are closely monitored and managed. Information is presented to users in a more useful format. There remains scope to develop reports, linking finance and performance more closely to aid decision-makers. The Council produces objective and balanced summary reports for the public and makes them easily accessible.

30 To support the Council's continuing improvement, I have focused my recommendations on key areas that will help the Council face the significant challenges it faces. My earlier Annual Governance Report contained the following recommendations along with the Council's response:

- further develop procurement across all of the Council, as this is a key factor that will determine the savings it can achieve and the impact of any changes on services and the local community;
- timely implementation of asset management plans;
- develop asset management benchmarking and performance indicators; and
- link financial and performance information more clearly in reports to aid decision-makers.

National Fraud Initiative

31 The Council has taken a pro-active approach to following up data matches arising from the latest National Fraud Initiative (NFI) data-matching exercise. Following investigation, the Council is taking action to recover payments totalling £64,443 due to fraud and error, including some large value benefit frauds. This compares to savings of £52,081 from the previous exercise.

32 Had these frauds and errors not been identified, the Audit Commission has estimated the cost would have totalled up to £150,000.

Approach to local value for money work from 2010/11

33 Given the scale of pressures facing public bodies in the current economic climate, the Audit Commission has been reviewing its work programme for 2010/11 onwards. This review has included discussions with key stakeholders of possible options for a new approach to local value for money (VFM) audit work. The Commission aims to introduce a new, more targeted and better value approach to our local VFM audit work.

34 My work will be based on a reduced number reporting criteria, specified by the Commission, concentrating on:

- securing financial resilience; and
- prioritising resources within tighter budgets.

35 I will determine a local programme of VFM audit work based on my audit risk assessment, informed by these criteria and my statutory responsibilities. I will no longer be required to provide an annual scored judgement relating to my local VFM audit work. Instead I will report the results of all my local VFM audit work and the key messages for the Council in my annual report to those charged with governance and in my annual audit letter.

Current and future challenges

Current challenges

36 Local government is facing major operational and financial challenges. The Treasury announced £6.2 billion of in-year savings from Government spending on 24 May 2010. The Communities and Local Government department will make the biggest proportionate contribution of 12.5 per cent (£780 million), with local government contributing 6.5 per cent (£405 million).

37 £1.2 billion of savings is being made in 2010/11 by reducing grants to local authorities. The main impact on revenue grants for the Council in 2010/11 is a reduction of £2.2 million.

38 The Government has also announced reductions in capital expenditure following a fundamental review of all streams of capital expenditure. The single biggest impact on the Council of capital expenditure cuts is the cancellation of the Building Schools for the Future programme. The Council was expecting funding of £95 million for buildings work of which only £12.4 million will now be received in respect of Dyke House school refurbishment. A further £8.8 million was expected for ICT infrastructure and the Government has confirmed this will go ahead as planned.

39 Robust financial management to maintain a stable financial position will be increasingly important and the Council's improvements in financial management in recent years will support this. Local area agreements and the national performance indicator set have been abolished. The Council will need to consider what performance management information it will need in order to ensure good performance management, monitoring changes in demand and the impact of budget changes on delivery.

40 The Council's partners are also changing. The Government has announced that it plans to devolve responsibilities for commissioning health care from Primary Care Trusts to local GP Commissioners. More schools may opt to become academies or foundation trusts and there may be free schools set up in the Borough.

41 In response to the funding reductions and changes, the Council has continued to review its medium term financial plan. It has already begun analysing options for responding to the predicted cuts including modelling on different levels and timings when funding reductions might happen ahead of the recent October spending review. The Council's Business Transformation Programme, with its Service Delivery Options should provide the organisational framework to support the review of services. The Council has made good progress with this Programme which is largely on track, with planned full year savings of £2.9 million in 2010/11 compared to the original estimate of £1.3 million.

Future developments

42 The Government's spending review was published on 20 October 2010, setting out revenue and capital spending plans for each government department from 2011/12 to 2014/15. Local authorities face significant cuts.

43 The Government has also set out its ambition to promote the radical devolution of power and greater financial autonomy to local government and community groups which would include a review of local government finance. Along with this focus on 'localism', councils are to be given a new power of 'general competence'. The review of local government finance will start in summer 2011 with findings due to be published in 2012. This review could, therefore, potentially inform local government finance settlements from 2013/14.

44 In addition, the Local Government Boundary Commission has carried out an electoral review of the Council. It has approved a new Council size of 33 members instead of the current 47 and is now consulting on ward boundaries. Having reduced its management capacity in the recent restructure, the Council will need to review the impact of these reductions. Members and officers will need to ensure there is a streamlined, robust and well focused governance framework and approach. This will help the Council meet the significant challenges it faces, with some potentially very difficult decisions to make.

Closing remarks

45 I have discussed and agreed this letter with the Chief Executive. I will provide copies to all Council members and will present this letter at the Audit Committee on 3 December 2010.

46 Full detailed findings, conclusions and recommendations in the areas covered by our audit were included in the reports I issued to the Council during the year.

Report	Date issued
Certification of grants report for 2008/09	March 2010
Audit fee letter for 2009/10	April 2009
Opinion Audit Plan	June 2010
Annual Governance Report	September 2010
Opinion on the financial statements	September 2010
Value for money conclusion	September 2010
Annual Audit Letter	November 2010

47 The Council has taken a positive and helpful approach to our audit. I wish to thank Hartlepool Borough Council staff for their support and cooperation during the audit.

Lynne Snowball
District Auditor

November 2010

Appendix 1 Audit fees 2009/10

	Actual	Proposed	Variance
Financial statements and annual governance statement	£171,593	£171,593	£0
Value for money	£90,729	£90,729	£0
Total audit fees	£262,322	£262,322	£0
Total	£262,322	£262,322	£0

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. It includes how the Council 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 accounts, auditors must give their 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;
- whether they have been prepared properly, following the relevant accounting rules; and
- for local probation boards and trusts, on the regularity of their spending and income.

Financial statements

The annual accounts and accompanying notes.

Qualified

The auditor has some reservations or concerns.

Unqualified

The auditor does not have any reservations.

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 money, people and time.

If you require a copy of this document in an alternative format or in a language other than English, please call:
0844 798 7070

The Statement of Responsibilities of Auditors and Audited Bodies issued by the Audit Commission explains the respective responsibilities of auditors and of the audited body. Reports prepared by appointed auditors are addressed to non-executive directors, members or officers. They are prepared for the sole use of the audited body. Auditors accept no responsibility to:

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

Audit Commission

1st Floor
Millbank Tower
Millbank
London
SW1P 4HQ

Telephone: 0844 798 3131
Fax: 0844 798 2945
Textphone (minicom): 0844 798 2946

www.audit-commission.gov.uk November 2010

AUDIT COMMITTEE

3 December 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Head of Audit and Governance

Subject: INTERNAL AUDIT PLAN 2010/11 UPDATE

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1. PURPOSE OF REPORT

1.1 To inform Members of the progress made to date completing the internal audit plan for 2010/11.

2. BACKGROUND

2.1 In order to ensure that the Audit Committee meets its remit, it is important that it is kept up to date with the ongoing progress of the Internal Audit section in completing its plan. Regular updates allow the members of the Committee to form an opinion on the controls in operation within the Council. This in turn allows members of the committee to fully review the Annual Governance Statement, which will be presented to a future meeting of the Committee, and after review, will form part of the statement of accounts of the Council.

3. AUDITS COMPLETED AND IN PROGRESS

3.1 **Appendix A** of the report details the pieces of work that have been completed.

3.2 As well as completing the afore mentioned audits, Internal Audit staff have been involved with the following working groups:

- Information Governance Group.
- Procurement Working Group.
- Performance and Risk Management Group.

3.3 The section has now coordinated the upload of all required information to the Audit Commissions secure website in relation to the National Fraud Initiative (NFI) for 20010/11.

3.4 We received notice on the 16.11.10 that the Government has decided to end the current Financial Management Standard in Schools (FMSiS) with immediate effect and develop a simpler standard as a replacement. As we have been undertaking the FMSiS assessment as part of our normal audit coverage we have informed schools that we propose to undertake the following actions:

- Stop FMSiS assessments immediately,
- Carry on with our programme of internal audit coverage in schools as planned taking out specific FMSiS related issues,
- Not charge for FMSiS assessments already carried out this financial year.

3.5 **Appendix B** details the audits that were ongoing at the time of compiling the report.

4 AUDIT PLAN PROGRESS

4.1 The work completed and currently ongoing is in line with expectations at this time of year, and audit coverage to date has allowed the Audit Commission to place reliance on the scope and quality of work completed when meeting their requirements under the Audit Code of Practice.

5 RECOMMENDATION

5.1 It is recommended that Members note the contents of the report.

Appendix A

Audit	Objectives	Recommendations	Agreed
Integrated Care Management Board	The partnership has a clear strategy/purpose, based on need identified in consultation with community and service users. Roles and responsibilities of partners are clearly defined and documented with appropriate mechanisms in place to ensure both internal and external accountability to stakeholders. Communication and consultation mechanisms are in place. The partnership has adopted formal procedures governing the conduct of the business and defining the standards of personal behaviour to which individual members, officers and agents are required to subscribe. Standards are documented and clearly understood. The partnership has a defined performance management system in place to enable monitoring and reporting of progress against its specified objectives. Responsibilities for the partnership's financial management are clearly defined including monitoring and reporting arrangements. There are suitable systems and controls in place to ensure financial resources can be accounted for. The partnership has an effective risk management system in place to ensure that key risks to the achievement of partnership objectives are identified and managed effectively. Effective HR arrangements are in place that considers the aims of the partnership, identify the range of skills required, and translates this into a plan covering resource requirements, functions and expertise required, ensuring that robust procedures for the recruitment & selection of staff, effective performance appraisal systems and appropriate training and development are in place. Information sharing protocols for the partnerships are clearly defined including ICT systems. The partnership has implemented procedures to meet FOI 2000 and DPA requirements. The	- The partnership should agree a long term strategy document which sets out the purposes and scope of its work and the responsibilities of each partner organisation. Approval should be recorded in the minutes of the board meetings. All stakeholders should be involved in developing the long term strategy. Partnership objectives should be in accordance with the long term strategy and other relevant plans and priorities and focus on outcomes and activities. Milestones /targets should be agreed by the board to determine progress against the achievement of objectives. The board should be presented with performance monitoring reports on a regular basis. There should be a Risk Management Policy in place setting out the overall framework within which the whole organisation must work and defining responsibilities and accountabilities. The policy should require risk management to be embedded into the organisation's strategic and annual planning processes. The partnership should have a risk register which defines: Gross risk; Mitigating actions; Net risk; Risk ownership; Regularity of reviews. The financial plan should clearly set out the sources of funding expected to deliver the strategic objectives including how much each partner will contribute and factors for expected inflationary costs. The plan should include a clear assessment of cash flow requirements and how these will be met. There should be an exit strategy in place which sets out the procedure/ protocols required to withdraw from the arrangements which addresses the following areas; period of notice, asset ownership, distribution of partner contributions, personnel issues - TUPE and redundancy, IT issues - system and data transfers, who needs to be informed - customers funders insurers, information security, likely impact of the partnership winding up, resources required to assist with this process. Contingency plans should be developed for if one or more organisations withdraw from the partnership. - There should be a partnership	Y Y

	partnership has suitable arrangements in place to ensure value for money is obtained when procuring goods and services. Ownership of assets is clearly defined including arrangements beyond the lifetime of the partnership. Any assets held by the partnership are suitably managed and controlled.	agreement in place, which has been signed by all partner agencies and covers the following areas; name of partnership, aims and objectives, what partnership is set up to do, membership, including status termination arrangements scheme of delegation, powers - how the partnership will achieve aims, roles, income, meetings - notice frequency quorum rules chairing voting representation, decision making process, timescales, amendments to rules - what happens if change is required, minutes, reporting, exit strategy. The partnership agreement should contain conditions that require formal regular assessments of the partnership's membership to ensure that any expertise available/needed can be brought in. The partnership should have a communication strategy in place with a range of channels to interact with; internal - partner agencies/representatives/staff/ councillors/newsletters/agendas /meetings, external - service users/ public / media/business/well publicised meetings held in public, use of local media to promote work of the partnership and invite contributions from the general public/website. The strategy should be reviewed on a regular basis. There should be formalised arrangements in place for receiving and responding to complaints. - That a code of conduct is in place which is signed by all staff/ members. That the partnership has arrangements in place to ensure that diversity issues are considered. That partners have agreed to abide by a specific set of Financial Procedure Rules. That there is a scheme of delegation to ensure that officers expend within limits. That members/ officers with purchasing power have signed a register of business interests. That declarations of interest are made on a regular basis to enable emerging interests to be recorded.	 Y
Ward Jackson Primary	Ensure school financial and governance arrangements are in line with best practice.	- The school should prepare a SIC for the financial year ended 31/3/2011 using this internal audit report as a source of assurance on the risk / control position. - As well as identifying individual training needs, Members of the	Y Y

		Governing Body (and in particular Finance) should evaluate their strengths in order that the school may utilise these competencies. Where training needs are identified that appropriate training is provided to ensure that the school has the full range of competencies available. Records of training provided should be maintained by the school. - A register of business interests (including 'nil' returns) should be maintained for all governors and those staff who can influence purchasing decisions. The register should be updated at least annually. - All items of equipment costing in excess of £500 or of a portable and attractive nature should be recorded in the inventory record. Records should include Serial numbers etc. Annual reconciliation of assets to records should be undertaken by a person independent of the maintenance of inventory records. - A self evaluation of staff financial management competencies should be carried out by the HeadTeacher and School Secretary and any other member of staff with a financial role to ensure that the financial competencies required by the school are in place. Such staff should be given the opportunity to attend financial management training courses particularly to address any gaps in their competencies. All training records should be maintained on file. - A self evaluation of staff financial management competencies should be carried out by the HeadTeacher and School Secretary and any other member of staff with a financial role to ensure that the financial competencies required by the school are in place. Such staff should be given the opportunity to attend financial management training courses particularly to address any gaps in their competencies. All training records should be maintained on file. - The Governing Body should ratify the LEA's Financial Regulations which should be reviewed on a regular basis (at least two yearly) an electronic version of LEA financial regulations is attached with this report. - The Governing Body should formally adopt a scale of charges which should be reviewed on an annual basis.	 Y Y Y Y Y Y

		- The school should consider its insurance limit when collecting and banking monies for the private fund and ensure that such limits are not exceeded. - In order to demonstrate Best Value in the provision of its services the School should identify areas to review the economic, efficient and effective use of resources, document these areas in a best value statement and submit this statement to the LEA on an annual basis. - The school should develop detailed local procedures for the finance function and ensure that they are approved by the Governing Body. A model financial procedure document is attached to this report and the school may consider adapting this document to fit its particular circumstances. - Risk management should be embedded into the schools processes. This can be achieved by: Establishing a risk management group to co-ordinate the school's risk management activities; Providing appropriate training in risk management to the group; Undertaking risk assessments of all school activities to identify, evaluate and treat risks to the achievement of school priorities. The school may utilise the risk management software provided by internal audit in order to carry out annual reviews of the school's risk position and inform the preparation of the school's annual Statement of Internal Control. Training in the use of the software can be provided by Internal Audit. - All staff with access to personal data should complete a data protection form of undertaking. - Records should be maintained by the school of all software loaded onto desktop machines / laptops etc. Regular software audits should be undertaken by the school to ensure that unauthorised software has not been installed on machines and that the number of software licences retained agrees to the software loaded onto machines. - The Governing Body should classify its information assets (both electronic and paper based information) and agree a publication scheme (see model publication schemes) and access policy in accordance with the	Y Y Y Y Y Y Y

		Freedom of Information Act. - Back ups should be made and checked to ensure if there was an IT failure then information can be restored. Back ups should be stored in a secure location within the school away from the main computer/server. For Data Protection reasons back ups should not be taken off the premises. - There should be examination of the annual accounts of the private fund by an independent person. Annual accounts that have been subject to such examination should be presented to the Governing Body. - All private funds maintained by the school should have a constitution, which is approved by the Governing Body, and details the purpose of the fund and arrangements for its management. The School should appoint a person independent from the day to day administration of the school fund to examine the year end financial statements. Annual accounts should be presented to the Governing Body. In order to reduce administration burden, the school should consider merging the two funds into one. - Checks should be undertaken to ensure that salary costs recorded on the contracts Information on SIMS agree with actual salaries. - Appropriate checks should be undertaken on all new Governors. CRB clearances should be reviewed every three years. - Orders should be used for all goods and services with a few limited exceptions. These orders should then be committed on the school's financial system to prevent overspending. - Import files are uploaded regularly to ensure effective and up to date budget monitoring. - The School Improvement Plan should be reviewed and updated to include financial priorities to comply with DfES guidance.	 Y Y Y Y Y Y Y Y
Libraries	Procedures are in place to protect assets and data, income collected is securely held and banked promptly, internet security is maintained, no group of users are excluded from or has difficulty using the library, regular stock checks are carried out and a inventory is maintained.	- Community room hire charges should be reviewed and approved annually. - All library branches should be made aware and receive formal notification of the change in charges prior to the start of the new financial year. - All drivers should obtain CRB clearance prior to working on the mobile and home library service. Checks should be renewed every three years with evidence being retained –	Y Y Y

		i.e. copy of email from Human Resources.	
Capital Accounting	Examine and evaluate the adequacy of controls in place to ensure the accuracy, validity and completeness of the asset register and accounting records.	- Procedure notes are drawn up documenting the processes in place for carrying out valuations - from identifying when valuations are required to notification of changes in valuations to the Finance Division. The sales and purchases processes also require documenting. - Consideration is given to using departmental inventories to cross check to the Finance Asset Register as a method of confirming accuracy and ensuring that assets have not been disposed of without the required authority, following an assessment of the departmental inventories by Internal Audit. - That all assets are allocated a unique reference number which enables the asset to be traced from 'cradle to grave' i.e. when it first becomes an asset to when it is disposed of. This should provide a method of identifying any additions or deletions.	Y Y N
Budgetary Control	The roles and responsibilities for key officers and budget holders are clearly defined and those staff have received adequate budget training. Budgets are set in accordance with pre-determined approved policy objectives. The budget setting process is supported by a risk management framework. Documentary evidence supports the make up of the budget. Budgets are prepared promptly in line with the annual budget process and timetable. All relevant records are correctly up dated with the budget set and approved. Working papers adequately support the budget loaded into the ledger. Budgets set are reported annually to the managing body prior to implementation. Budget amendments of a significant nature are reported to and approved by the managing body. Budgets are properly controlled through effective monitoring arrangements in accordance with Financial Procedure Rules. There is an established financial risk management process to determine the level of reserves.	None	
Main Accounting System	Financial management arrangements, accounting	- That care is taken to ensure that personal details are not entered onto	Y

	standards and policies adopted by HBC meet the requirements of the organisation, comply with legislation and best practice and are adhered to throughout the organisation. The financial accounting system is sufficiently robust and flexible enough to meet the needs of different users (i.e. budget holders, senior managers, those charged with governance), capable of expansion to meet any growth in the organisation or in its financial information requirements. All transactions recorded in feeder systems are completely and accurately transferred to the main accounting system. Accounting balances from the previous financial year are brought forward into the current years accounts correctly. Transactions within the main accounting system are correctly coded and calculated. The output from the main accounting system is correctly presented in the authority's final accounts. The security and integrity of the system is maintained.	the financial management system as these may be made available to officers who would not normally be able to view such information. There may also be data protection issues. - All officers responsible for inputting journals should be reminded of the need for all input documents to be marked as processed once the transaction is complete. - The description on journals should be sufficient to establish why the transaction has taken place or provide a link to more detailed information.	 Y Y
Business Transformation Process	Evaluating the effectiveness of the arrangements in place to mitigate risks in the following areas: Strategy/Policy Arrangements, Performance Management, Accounting Arrangements and Communication.	- That the Communication process used currently is reassessed based on feedback from stakeholders.	Y
Computer Audit	Ensure adequate controls over the use and security of emails and the internet are in place.	- The new internet/email policy should state who keeps a copy of the signed forms of undertaking. - The Internet & Email Policy states that "compliance with this policy will be undertaken within each departments standard monitoring arrangements, including monitoring of flexitime sheets, time sheets, time recording systems etc". The policy should be amended to say compliance should be monitored within normal management routines in departments, to reflect what is currently in place. - Once the draft policies are approved these should be circulated to all staff that have access to the Internet and or email. - Northgate should identify which schools are using a generic User ID and ensure they are changed and	Y Y Y Y

		each member of staff that requires access has there own user ID.	
14 – 19 Education	Ensure adequate arrangements are in place that cover the following areas: Governance arrangements; Strategic / operational planning; Service delivery; Legislation; Performance management; Use of resources.	- Terms of reference should define attendance levels require to enable meetings to be quorate. - Members of the Board should complete annual declarations of interests, including 'nil' returns. - The operational plan should include: actions broken down into deliverable short term milestones to enable regular monitoring and the early identification of barriers to achievement. Such milestones should be monitored by the relevant task group with exceptions reported to the Board on a regular basis. Financial / other resources required to deliver actions should be considered in operational planning documents by including costings where appropriate; analysis of relevant data / consultation used to inform operational activities. - Membership of the task groups should be established and formally documented in terms of reference. The terms of reference should also define the order of business of meetings and include a requirement to review progress against established milestones designed to implement operational plan actions and report potential barriers to the Strategic Board for consideration.	Y Y N N
Officers Expenses	Ensure that all expenses claimed are accurate, valid and in line with Council policies.	- A review of officers with the ability to process employee expense claims through Integra is performed and updated where necessary. - Steps are taken to ensure reset claim amounts cannot be overridden by users and can only be amended by designated officers within the Finance Team. - The auditor obtains copies all the relevant insurance certificates and tests as part of the follow up audit. - Officer Expense claim processes are included as an item with the Integra User Group and the process discussed with departmental representatives to ensure all are updated in the process of submitting claims and what documentation needs to be seen and retained. - System parameters should prompt officers to verify sight of receipts. - All rate updates should be logged, signed and dated by the inputter and the checker.	Y Y Y Y Y Y

		- The Travel Arrangements information sheet available to staff via the Intranet is updated by Central Procurement to request that staff must include the reason why they have used an alternative provider when submitting their claim forms (i.e. by writing on the claim form who the alternative provider is and why they were used e.g. better price). - Departments are reminded of the need to follow the criteria set out in the scheme and reimbursements of subsistence are as per the rates within the scheme. - A casual car mileage procedure is made available to staff which sets out the appropriate rates and criteria/ documentation required when submitting claims and the process which is to be followed by all staff involved in the processing of paperwork. - Departments are made aware of the importance of ensuring that all information required on claims has been completed correctly prior to processing. Incomplete forms/ discrepancies should not be processed and be returned to the relevant staff.	Y Y Y Y
Foreshore Management	Arrangements for identifying and complying with relevant legislation specific to the service are in place.	- The service should consider establishing links with relevant internal and external stakeholders to promote the most effective management of the Foreshore and ensures: Health and safety; Access restrictions; Water quality through anti pollution measures; Contingency planning; Integrating beach activities into Tourism strategies; Transport links to beach areas. - A Coastal Strategy should be developed (or incorporated into the strategy document currently under development) which sets out the Council's vision for the future, provide a map for change and demonstrates how the community and council wish to see the coastal environment be protected, used and managed in the future. Such a vision should be developed following necessary consultations with the public, associated stakeholders (see previous section) and legislative requirements and include: Consideration of current tourism strategies to ensure it compliments	Y Y

		and enhances Council objectives to promote tourism; Results of consultation exercises undertaken with the general public and other interested parties; Arrangements for implementing the vision; Foreshore objectives derived from the vision; Arrangements for implementing the vision. - Benchmarking exercises should be undertaken to determine the rate neighbouring authorities charge for beach side "rights". Consideration should then be changing arrangements for seeking bids to attract a wider range of providers through different methods of advertisement and including a 'minimum price' for bids based upon 'going rate'. - The service should seek advice from Human Resources as to whether providers of 'various rights' should be subject to enhance CRB disclosure as part of preliminary checks. - Customer satisfaction surveys should be issued to residents / tourists with a view to gauging public opinion on services provided.	Y Y Y
Stranton Primary	Ensure school financial and governance arrangements are in line with best practice.	- All recruitment documentation should be retained by the school for a period of at least 6 months. - The Governing Body should classify its information assets (both electronic and paper based information) and agree a publication scheme (see model publication schemes) and access policy in accordance with the Freedom of Information Act. - Periodic reviews should be undertaken every three years of all governors to obtain up to date CRB clearance. - Income records are amended to include the total amount collected for the week and also the date banked to enable reconciliations to be performed. - To ensure the school comply with FMSiS requirements, more governors complete the evaluation (i.e. members of the Finance Committee). As FMSiS requires that the school is not reliant on one person and to ensure the Governors perform the role of critical friend and effective participation from other governors is required. - Checks should be undertaken to ensure that salary costs recorded on	Y Y Y Y Y Y

		the contract information on SIMS agrees with actual salaries. - The School Development Plan should be based upon 3 to 4 years instead of annual in order to comply with DfES guidance. - Debts exceeding £20 should be referred to the LEA in order that recovery action can be taken. - Contract Procedure Rules should be followed when acquiring goods/ services in excess of £5000. Records of contract evaluation and decision to award should be signed by officers involved in the process, retained and the decision reported to the Governing Body. - The school should develop detailed local procedures for the finance function and ensure that they are approved by the Governing Body. - Risk Management should be embedded into the school's processes. This can be achieved by: • Establishing a risk management group to co-ordinate the school's risk management activities; • Providing appropriate training in risk management to the group; • Undertaking risk assessments of all school activities to identify, evaluate and treat risks to the achievement of the school's priorities. The school may utilise the risk management software provided by Internal Audit in order to carry out annual reviews of the school's risk position and inform the preparation of the school's Statement of Internal Control. - All staff with access to IT systems should complete a data protection for of undertaking.	 Y Y Y Y Y Y
St Begas Primary	Ensure school financial and governance arrangements are in line with best practice.	- Minutes of all F&GP Committee should be retained in a secure manner. • The F&GP Committee should adopt the model of minutes used by the full governing body with resolutions of the committee clearly stated. Standing agenda items that are consistent with the agreed terms of reference should be included for all meetings. • An action column which defines responsibility for implementing governor decisions should be included. • Effective clerking arrangements should be in place for the Committee as required by part 4 of the Statutory Guidance on the School Governance	Y

		(Procedures) (England) Regulations 2003. This guidance states that the HeadTeacher cannot be a clerk, although a member governor can be appointed. It is considered best practice to appoint a qualified clerk (or who is receiving training).	
		- The Governing Body should undertake a review of the schools control environment and prepare / sign a Statement on Internal Control which reflects the guidance issued by DfE. Any material weakness in the control environment of the school should be reflected in the wording of the SIC. This internal audit report and action plan should be used to inform the production of a Statement of Internal Control.	Y
		- That the remaining recruitment testing is carried out by the auditor during the audit follow up.	Y
		- A self evaluation of staff financial management competencies should be carried out by the HeadTeacher and School Secretary, using DfE competency grids. Such staff should be given the opportunity to attend financial management training courses, particularly to address any gaps in their competencies and records maintained of any training provided.	Y
		- That the corrections are made and the information on SIMs kept up to date to ensure that the budget information is accurate.	Y
		- Arrangements put in place to formally document the process of evaluating applications for vacancies against the essential and desirable criteria for the post and also the evaluation of interview results. These forms are available through the Recruitment Guidance.	Y
		- The GB should carry out a review of the staffing structure and consider benchmarking results which compare staffing costs.	Y
		- That budget monitoring reports are supported by the appropriate SIMs report.	Y
		- That the results of the benchmarking exercise are analysed and fed back to governors, the governor's consideration of the benchmarking results should be minuted.	Y
		- That the Head and Governors ensure that regular reports on the projected outturn continue to be taken to	Y

		Governors and that these are minuted. Also that this is reviewed further by Internal Audit at the follow up audit as maintaining the repayment of the deficit will impact on whether the standard can be awarded.	
		- That the SDP is reviewed to include 3 years forecasting information and governors review progress on implementing the actions in the SDP on a regular basis and this is minuted.	Y
		- Financial Regulations should be approved by the governing body.	Y
		- That procedures are put in place to ensure that all cash passed between members of staff is signed for by both parties.	Y
		- Procedures are drawn up for the recovery of school meal debt, which should incorporate recording all contact with parents regarding the outstanding debt and the various stages of the process to ensure consistency.	Y
		- Arrangements are put in place to ensure that the school bank account is not allowed to go overdrawn.	Y
		- Quotations are obtained for expenditure above £5,000, this expenditure should also have been approved by the Chair/Vice Chair as per the Terms of Reference of the Finance and General Purposes Committee.	Y
		- Governors should be formally made aware of any potential conflicts of interest.	Y
		- That further explanation is provided regarding the payment made and no cheques are signed without the appropriate supporting documentation being in place.	Y
		- All orders should be raised at the time the items/services are requested as this enables committed expenditure to be accounted for when monitoring the budget - this is particularly important given that the school is operating with a deficit budget.	Y
		- That the inventory be updated to include serial numbers, make, model, date of purchase, value where appropriate. This could be held in an electronic format.	Y
		- That the Local Financial Procedures are reviewed and expanded to meet the requirements of the FMSiS. These should be approved by the Governing Body and distributed to all appropriate staff.	Y

		- That invoices are paid within the terms and conditions. - Risk management should be embedded into the schools processes. This can be achieved by: Establishing a risk management group should to co-ordinate the school's risk management activities; Providing appropriate training in risk management to the group; Undertaking risk assessments of all school activities to identify, evaluate and treat risks to the achievement of the schools priorities. The school may utilise the risk management software provided by internal audit in order to carry out annual reviews of the school's risk position and inform the preparation of the school's Statement of Internal Control. - The school should have an ICT strategy in place which provides direction in the use of ICT resources in the areas of learning, teaching and administration. - An internet policy should be made available to parents, and permission sought to enable children to access the internet. The Policy should also be approved by Governors. - Back ups should be stored in a secure location within the school away from the main computer/server. Back ups should be tested and evidence of such should be maintained. - Records should be maintained by the school of all software loaded onto desktop machines / laptops etc. Regular software audits should be undertaken by the school to ensure that unauthorised software has not been installed on machines and that the number of software licences retained agrees to the software loaded onto machines. - The Governing Body should classify its information assets (both electronic and paper based information) and agree a publication scheme (see model publication schemes) and access policy in accordance with the Freedom of Information Act. The access policy should require all subject access requests to pass through the HeadTeacher or nominated co-ordinator. Staff should be instructed not to pass information assets out of the school. - Private Fund records should be reconciled with each bank statement	Y Y Y Y Y Y Y Y

		received and a record made that this has been completed. - That year end financial statements are produced for the private fund and reported to Governors and parents. - That all income and expenditure transactions can be supported by documentary evidence. - That further testing is carried out by the Audit Section on the Private Fund. - That the bank mandate is updated.	 Y Y Y Y

Appendix B

Audit	Objectives
Integrated Transport Unit - Workshops	Procedures are in place to ensure identified risk is mitigated in achieving the objectives of the workshops.
Creditors	Ensure that Supplier accounts are raised promptly, accurately and only when they do not already exist or when the raising of such suppliers would breach corporate contracts in place at the authority. Controls are in place to prevent the amendment of supplier accounts for fraudulent purposes. Official orders are raised to purchase goods and/or services unless in exceptional circumstances. Payment is only made for goods and/or services received with sufficient evidence retained that checks are made to ensure that goods are received in full and of the appropriate quality. Arrangements are in place to ensure that payments are made promptly, and any discrepancies that prevent the prompt payment are resolved in a timely manner. Processing controls are robust and ensure that all payments are fully processed. The payment process is secure. A management trail is in place to enable financial transactions to be vouched from source to payment.
Transport Plan	Ensure adequate arrangements are in place for compiling the Transport Plan, Funding arrangements, budget allocations and budgetary control processes, performance management and sustainability.
Fraud Awareness	To evaluate the awareness of fraud across the Authority considering the following areas: Newsline, Management Matters, Payslips, Article in Hartbeat, Council Tax Leaflet and Trading Standards. Identify any gaps. Complete the 'Managing the Risk of Fraud' checklists covering: Adopting the Right Strategy, Accurately Identifying the Risks, Creating and Maintaining a Strong Structure, Taking Action to Tackle the Problem, Defining Success. Examine Corporate Risk Register re: Risk of Fraud.
Debtors	The audit has focused on the following areas: - Creation of debtor accounts to ensure that debts for one individual are all in the same account and that the accounts contain sufficient detail to enable effective recovery action to be taken. - Raising of both invoices and credit notes to ensure that they are accurate, timely and authorised. - Allocation of payments to the accounts to establish that the processes in place provide assurance that the payment is accurately and timely allocated to the correct invoice. - Recovery of debt outstanding to ensure that all debt due to the authority is effectively followed up to reduce the amount of debt owing and only written off as a bad debt where all recovery avenues have been exhausted.
Capital Programme	Ensure that there is a strategic approach to allocating capital resources which links to the Authority's overall aims and objectives. Determine and evaluate the methods in place for prioritising schemes/projects. Examine the arrangements in place for obtaining financing for the capital programme to ensure that all agreements entered into are appropriately authorised. Evaluate the processes in place for allocating and monitoring funding made available for specific projects/schemes. Ensure that there are robust processes in place for monitoring spend against the capital programme and reporting on any issues arising.
BSF/PCP	To provide assurance that arrangements in place will successfully deliver both the BSF and PCP programmes. It was not intended to review individual projects carried out under the schemes. Due to cessation of the BSF programme, the audit focussed on the Primary Capital Programme and involved reviewing the following areas: Strategy development; Governance; Development and delivery of the BSF / PCP programmes; Budgetary control; Risk management.

SIMS School System	There are effective procedures in place for the SIM's system. Children's Services, Accountancy and Schools are all fully aware of their responsibilities surrounding the SIM's System. There are comprehensive arrangements in place for effective budget setting in SIM's & INTEGRA. Effective arrangements in place surrounding import files and coding within SIM's. Regular reconciliations are carried out between SIM's and Integra. Effective arrangements in place for posting of Income. Effective personnel arrangement in place at schools. Effective security arrangements are in place.
Wrap Around Care Provision	Review the arrangements in place within schools for establishing wrap around care provision and ensuring that they operate in a sustainable manner and all appropriate action taken to comply with legislative requirements.
Direct Payments	To ensure all payments made are done so in a controlled way ensuring compliance with good practice and legislation.
VAT	The aim of the audit was to review the arrangements in place for administering VAT to ensure that that staff involved in the processing of VAT are aware of their responsibilities, VAT categories are correctly identified accounted for, and effective planning ensures efficient, effective and economic operations which maximise benefits to the Council.
Council Tax	Evaluate the adequacy of systems and procedures in place to ensure that: All taxable properties are identified, assessed and recorded and these records are accurately maintained; All persons liable for council tax and all discounts, exemptions, benefits and other allowances have been identified and correctly recorded; Amounts due in respect of each taxable property have been correctly calculated and promptly demanded from the person(s) liable; Secure and efficient arrangements exist for all collections, which are promptly posted to the correct taxpayers' accounts. All refunds are authorised and valid; The billing authority complies with all statutory requirements for tax setting and the keeping of accounts.
Grange Primary	Ensure school financial and governance arrangements are in line with best practice.
Tees Archaeology	The focus of the audit review was to examine the arrangements in place of the shared service, in particular the areas relating to: • Responsibility and accountability. • Strategy and purpose. • Standards of conducts. • Performance management. • Financial management. • Risk management. • Staffing. • ICT security. • Contracts.
Petty Cash	Examination of guidance and procedures for petty cash and imprest accounts, the setting up, amending and monitoring of petty cash. Reimbursement and reconciliation of floats and imprest accounts. Authorisation of petty cash and reasonableness of expenditure. Review the security arrangements of floats and imprests.
Bailiffs	Bailiff Section have adopted relevant legislation and incorporated it into the internal Bailiff procedures. There are procedures in place to ensure all staff have undertaking Bailiff training. There are effective security arrangements in place for the collection, storage and banking of income.
NNDR	Review the following areas of operation in relation to NNDR: • Legislation, • valuation, • liability, • billing, • collection and refunds, • Security.
Employees Register of Interest / Gifts and Hospitalities	All council employees are aware of the need to disclose all pecuniary and other interests, including gifts and hospitality. Ensure that there is an adequate system in place for the disclosure and recording of all declarations of interest. Data is held securely and in line with the authority's policies and the Data Protection Act.

Social Care Transformation	Review procedures to ensure arrangements are in place that allow the Council to meet its commitments in terms of social care transformation responsibilities.
Cash/Bank	Review all cash transactions and the reconciliation process within the Cashbook Section of Accountancy in relation to direct debit payments, holding accounts, payroll and creditor payment transactions.
Tallships Income	Review income streams from parking permits and the various on site sales that were arranged (e.g. event guide sales).
Contracts/ Procurement	The audit focused on the Authority's Procurement Policy and Procurement Operations/monitoring and the tender processes undertaken to ensure that Contract Procedure Rules were being adhered to.

AUDIT COMMITTEE

3 December 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Head of Audit and Governance

Subject: INTERNAL AUDIT CHARTER

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1. PURPOSE OF REPORT

To inform Members of the updated Internal Audit Charter attached as **Appendix A** to the report.

2. BACKGROUND

2.1 In order to ensure that the purpose, authority and responsibility of Internal Audit is formally defined and consistent with the requirements of the Code of Practice for Internal Audit in Local Government in the United Kingdom, the Head of Audit and Governance must produce an audit charter.

2.2 The charter is effectively the terms of reference for Internal Audit and fulfils the following roles:

- Establishes the responsibilities and objectives of Internal Audit.
- Establishes the organisational independence of Internal Audit.
- Establishes the accountability and relationships between the Head of Audit and Governance and those charged with governance.
- Recognises that internal audits remit extends to the entire control environment.
- Require and enables the Head of Audit and Governance to deliver an annual audit opinion.
- Establishes Internal Audits right of access to all records, assets, personnel and premises, including those of partner organisations, and its authority to obtain such information and explanations as it considers necessary to fulfil its responsibilities.

3. RECOMMENDATION

That the Audit Committee approves the Internal Audit Charter.

Appendix A

HARTLEPOOL
BOROUGH COUNCIL

INTERNAL AUDIT CHARTER

Internal Audit

HARTLEPOOL BOROUGH COUNCIL

INTERNAL AUDIT CHARTER

1 INTRODUCTION

1.1 This document establishes the role and terms of reference of the Internal Audit function within Hartlepool Borough Council.

It has been framed to provide an effective internal audit service, to meet the needs of the Council and to accord with the requirements and guidelines of;

- Section 151 of the Local Government Act 1972;
- The Accounts and Audit Regulations 2006;
- The CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006;
- The Standards of the Institute of Internal Auditors.

1.2 It is the intention to review these Terms of Reference annually to ensure their relevance is maintained. Amendments will be subject to the agreement of the Section 151 Officer and Members of the Audit Committee.

2 *PURPOSE*

2.1 Internal Audit is an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment by evaluating its effectiveness in achieving the organisations objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources (*CIPFA Code of Practice for Internal Audit in Local Government in the United Kingdom 2006*).

2.2 To fulfil this role Internal Audit within Hartlepool Borough Council is required:

- To provide an annual written report to the Audit Committee which includes an opinion on the overall adequacy and effectiveness of the organisations control environment that supports the Annual Governance Statement;
- To review, appraise and report regularly on the soundness, adequacy and application of internal controls to management and the Audit Committee;
- To provide Management and Members of the Council with information, analysis, appraisal, recommendations, advice and assurance in order to assist them in the effective discharge of their responsibilities;
- To verify the existence and the means of safeguarding all assets;
- To plan audit work, having regard to this Charter, proper internal audit practices, the council's constitution and relevant statutes and regulations.

3 AUTHORITY

3.1 The authority of the Internal Audit function is derived from legislation mentioned in paragraph 1.1 and the Council's Constitution.

3.2 The requirement for an internal audit function for Local Authorities is implied by Section 151 of the Local Government Act 1972, which requires that Authorities "make arrangements for the proper administration of their financial affairs and shall ensure that one of their officers has responsibility for the administration of those affairs". The Accounts and Audit Regulations 2006 regulation 4, specifically require that "a review of the effectiveness of systems of internal control be considered by a committee of the relevant body" and regulation 6 requires relevant bodies to conduct an annual review of the effectiveness of its system of internal audit and for a committee of the body to consider the findings. Under the Councils constitution the Audit Committee undertakes this role.

4 *SCOPE*

4.1 The scope of Internal Audits remit covers the organisations entire control environment. This includes all of the Councils operations, resources, services and responsibilities in relation to other bodies.

4.2 The Head of Audit and Governance determines internal audit's priorities by preparation of a strategic audit plan based on assessed risk. This is reported to the Section 151 Officer, Corporate Management Team and the Audit Committee. In determining these priorities the Head of Audit and Governance takes into account the organisations assurance and monitoring mechanisms, including risk management arrangements.

4.3 In order to fulfil its role and be able to carry out their duties effectively, audit staff shall have access at all reasonable times to:

- All assets, documents, accounts, property, vouchers, records, correspondence and other information and data of the Council which are necessary for the proper performance of their duties. Such access shall be granted on demand and not subject to prior notice;

- Any Council employee or agency employee, to obtain information and explanations deemed necessary to form an opinion on the adequacy of systems and / or controls.

4.4 All officers and Members of the Council are required to render assistance to internal auditors in the conduct of their audits. These requirements are enshrined within the council's constitution.

4.5 It is management's responsibility to maintain the internal control system and to ensure that the Council's resources are properly applied in the manner and on the activities intended. This includes responsibility for the prevention and detection of fraud and other illegal acts.

4.6 It is the internal auditor's responsibilities to have sufficient knowledge of fraud to be able to identify indicators that fraud might have been committed. This knowledge includes the need to know that characteristics of fraud, the techniques used to commit fraud, and the types of fraud associated with the activities audited. An internal auditor should have regard to the possibility of such malpractice and should seek to identify serious defects in internal control, which might permit the occurrence of such an event.

5 INDEPENDENCE

5.1 Internal Audit will remain sufficiently independent of the activities that it audits to enable auditors to perform their duties in a manner which facilitates impartial and effective professional judgements and recommendations. Internal auditors have no operational responsibilities.

5.2 Internal Audit is involved in the determination of its priorities in consultation with those charged with governance. The Head of Audit and Governance has direct access and freedom to report in his own name and without fear or favour to all officers and members and particularly to those charged with governance.

5.3 Accountability for the response to the advice and recommendation of Internal Audit lies with management, who either accept and implement the advice or formally reject it. The outcome of all recommendations is reported to the Audit Committee for their consideration.

6 *RESOURCES*

6.1 Internal Audit must be appropriately staffed in terms of numbers, grades, qualification levels and experience, having regard to its objectives and to this Charter and Standards. Internal Auditors need to be properly trained to fulfil their responsibilities and should maintain their professional competence through an appropriate ongoing development programme.

6.2 The Head of Audit and Governance is responsible in conjunction with the CFO for appointing the staff of the Internal Audit Section and will ensure that appointments are made in order to achieve the appropriate mix of qualifications, experience and audit skills. The Section maintains an annually updated Training and Development Analysis Plan which sets out an ongoing development programme for Internal Audit staff.

6.3 The Head of Audit and Governance is responsible for ensuring that the resources of the Internal Audit Section are sufficient to meet its responsibilities and achieve its objectives. If a situation arose whereby he concluded that resources were insufficient, he must formally report this to the Chief Executive, the Section 151 Officer, and, if the position is not resolved, to the Audit Committee.

AUDIT COMMITTEE

3 December 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Head of Audit and Governance

Subject: INTERNAL AUDIT STRATEGY

1. PURPOSE OF REPORT

To inform Members of the updated Internal Audit Strategy attached as **Appendix A** to the report.

2. BACKGROUND

2.1 In order to comply with the requirements of the Code of Practice for Internal Audit in Local Government in the United Kingdom 2006 and the Accounts and Audit Regulations, the Head of Audit and Governance must produce an audit strategy.

2.2 The strategy attached updates the previous document and is a high level statement of how the internal audit service will be delivered and developed in accordance with its charter and how it links to organisational objectives and priorities. The strategy is included as part of the Internal Audit Manual and sets the context within which more detailed plans are developed.

2.3 The strategy communicates the contribution that Internal Audit makes to the council and includes:

- Internal Audit objectives and outcomes.
- How the Head of Audit and Governance will form and evidence the opinion on the control environment.
- How the service will be provided.
- The resources and skills required to deliver the strategy.

3. RECOMMENDATION

That the Audit Committee approves the Internal Audit Strategy.

Appendix A

HARTLEPOOL BOROUGH COUNCIL

INTERNAL AUDIT STRATEGY

AUDIT STRATEGY

Strategy Statement
The overall Strategy of Internal Audit is:

"To deliver a risk-based audit plan in a professional, independent manner, to provide the organisation with an opinion on the level of assurance it can place upon the internal control environment, and to make recommendations to improve it."

1 Statutory basis for Internal Audit

1.1 The requirement for an Internal Audit function for local authorities is implied by section 151 of the Local Government Act 1972, which requires that authorities "make arrangements for the proper administration of their financial affairs". The Accounts and Audit Regulations 2006 regulation 4, specifically require that "a review of the effectiveness of systems of internal control be considered by a committee of the relevant body"

2 Definition and Objective

2.1 Internal Audit is an assurance function that primarily provides an independent and objective opinion to the organisation on the control environment by evaluating its effectiveness in achieving the organisations objectives. It objectively examines, evaluates and reports on the adequacy of the control environment as a contribution to the proper, economic, efficient and effective use of resources (The control environment includes all authority operations, resources, services, and its responsibilities to other bodies).

2.2 To comply with the Accounts and Audit Regulations, the authority completes an Annual Governance Statement to demonstrate the robustness of its arrangements, and Internal Audit will form an important part of providing this enhanced assurance. Internal Audit also has a role in advising managers in relation to issues within its remit, e.g. appropriate controls in new projects/developments.

3 Status

3.1 Internal Audit is responsible to the Chief Finance Officer, for line management purposes. However, Internal Audit is independent in its planning and operation, and has no responsibility for delivering or managing non-audit services.

3.2 The Head of Audit and Governance shall have direct access to the Head of Paid Service (Chief Executive), all levels of management and elected members. Internal Auditors shall have the authority to:

- Enter at all reasonable times any Council establishment.
- Have access to all records, documents, information and correspondence relating to any financial and other transaction as considered necessary.
- Evaluate the adequacy and effectiveness of internal controls designed to secure assets and data to assist management in preventing and deterring fraud.

- Request explanations as considered necessary to satisfy themselves as to the correctness of any matter under examination.
- Require any employee of the Council to produce cash, materials or any other Council property in their possession or under their control.
- Access records belonging to third parties, such as contractors or partners, when required and appropriate.

4 Delivery of the audit service

4.1 The Head of Audit and Governance is responsible for delivering the audit service in accordance with its Charter. To ensure that this can be achieved, there are appropriate arrangements for:

- Determining and planning the work to be carried out (i.e. an audit plan based on an assessment of the risk);
- Providing the resources required to deliver the audit plan (principally the level of staff and external input), the necessary skills (both in general audit and technical areas) and support facilities (such as IT facilities, equipment and management and administration processes)

4.2 The Internal Audit service will be delivered on the basis of a Strategic Audit Plan which sets out the number of audit-days required for Internal Audit to adequately review the areas involved. The over-riding objective of this approach is to ensure that Internal Audit is able to present an opinion on the control environment by directing adequate resources based on the relative risks of the operations, resources and services involved, using a formal risk assessment process. The risk assessment process takes account of a range of strategic, corporate, service and operational risks (including those identified through the Risk Management process and by the external auditor) and the views of senior management on these issues. Where resources available are not considered by the Head of Audit and Governance to be adequate for such an opinion to be provided, this will be reported to the Chief Finance Officer.

4.3 The Plan balances the following requirements:

- The need to ensure the Audit Plan is completed to a good practice level (currently at least 90%);
- The need to ensure core financial systems are adequately reviewed to provide assurance that management has in place proper arrangements for financial control (on which External Audit will place reliance);
- The need to appropriately review other strategic and operational arrangements;
- The need to have uncommitted time available to deal with unplanned issues which may need to be investigated;
- To enable positive timely input to assist corporate and service developments.

4.4 A joint working arrangement with External Audit will be operated in order to ensure that Internal Audit resources are used as effectively as possible.

The Head of Audit and Governance will keep progress against the audit plan, and the content of the plan itself under review, in liaison with the Chief Finance Officer, and through monitoring corporate and service developments. Where there is a need for material changes to the plan (i.e. affecting over 20% of the planned assignments) a revised plan will be re-submitted to the audit committee for approval. The audit committee will also be advised of performance against the audit plan and on relevant indicators under the performance management framework.

4.5 Internal Audit will comply with the Auditing Practices Board's *Guidance for Internal Auditors*, as interpreted by CIPFA's *Code of Practice for Internal Audit in Local Government in the UK,* and staff are expected to comply with any other appropriate professional standards. The Head of Audit and Governance will ensure that there is an up to date *Audit Manual* in place setting out expected standards for the service, and will monitor compliance with these standards, including in relation to the planning, conduct and reporting of audit assignments. Relevant training will be provided to ensure auditors have the level of skills necessary to undertake their roles.

4.6 Where necessary to ensure an adequate, effective and professional audit service is provided; the Head of Audit and Governance will buy in resources from external providers to supplement internal resources. Internal Audit will aim to co-operate effectively with the external auditor and ensure that appropriate reliance can be placed on Internal Audit's activities.

4.7 The reporting approach for Internal Audit is set out in the audit manual and Internal Audit shall comply with this protocol as the most efficient method of delivering the outcomes of its work. In the delivery of each assignment, Internal Audit will look to make practical recommendations based on the findings of the work and discuss these with management such that management commit to an appropriate action plan for implementing any necessary improvements to the control environment.

5 Audit Environment

5.1 In order to ensure full and adequate audit coverage, the first step of audit planning will be the identification of the audit environment. This assessment will be made using knowledge, experience, discussion among the audit team, and liaising with finance and departmental directors.

6 Risk Assessment

6.1 Once the audit environment is identified, the Head of Audit and Governance will consider a risk assessment of each element of the environment. The Head of Audit and Governance will start audit planning by considering management's own assessment of risk, having first established that the risk register has been properly compiled and that it is a strong basis upon which to plan work. In order to assess the identified areas in terms of risk, the following factors have been adapted from CIPFA's risk assessment package to better fit the audit environment at Hartlepool:

- **System Factors**
  The stability and complexity of the system.
- **Managerial and Control Environment**
  Previous internal audit findings, client track record in responding, external audit comments, division of duties, perceived quality of staff, staff turnover and existence and quality of procedures.
- **Value of Transactions**
  The materiality of the total monetary value the population of the auditable area.

- **Volume of Transactions**
  The total population of transactions generated by the system.
- **Opinion Critical**
  The overall impact on the internal control environment opinion.
- **Legal Penalties**

The consequences of weakness leading to legal action.

6.2 Every auditable area will be allocated a mark out of 10 for each factor. The total score for each auditable area will be ranked, with the highest scoring areas being those facing the greatest risk. The following risk scores will dictate whether the auditable areas are subject to audit annually or to be reassessed the following year:

- Score 250 or more: annual coverage
- Score 249 or less: reassess annually

7 Resourcing the Plan

7.1 The Head of Audit and Governance will calculate the anticipated resources needed for the period under question. The calculation starts with the total available days, based on the number of staff in post and taking account of any staff movements. From this figure, allowances for annual leave, bank holidays and anticipated sickness are deducted to arrive at the number of productive days available.

7.2 Having obtained the results of the risk assessment process and determined the resources at the disposal of the Head of Audit and Governance, an audit plan for the period in question will be prepared. The plan will include a contingency provision to provide for tasks and reviews that were not foreseen when the plan was made or for emerging risks. The Head of Audit and Governance will determine whether the resources available are sufficient to allow a robust opinion on the state of the internal control environment. If, in the opinion of the Head of Audit and Governance, there are insufficient resources available, this will be reported to the Chief Finance Officer and/or the audit committee.

7.3 The likely outcome of such a report might include the provision of additional resources to review the identified risks or an acceptance that an increased level of risk must be borne by the authority. The Chief Finance Officer and audit committee will approve the plan.

8 Monitoring and Controlling

8.1 Effective management of the delivery of the audit plan is fundamental to ensuring that sufficient audit coverage is achieved. Factors that are taken into account include the timing of specific audits during the course of the year and the allocation of audits to those staff with the appropriate skills and experience to complete the task.

8.2 To help monitor and control the plan, all audit staff are instructed to complete timesheets held the automated software package used. The timesheets are to be completed on a daily basis with the work undertaken during that period using the codes identified for each area of work as listed in the annual audit plan. Analysis of staff time is produced by the time recording system, which allows comparison of actual output against the audit plan at individual, team and total level. The Head of Audit and Governance will prepare a summary report for the Chief Finance Officer and audit committee, outlining major variations and their impact on the ability of Internal Audit to complete its planned work for the year, stating clearly what effect this may have on its ability to measure the robustness of the authority's overall internal control environment for the period.

AUDIT COMMITTEE

3 December 2010

Report of: Head of Audit and Governance

Subject: ROLE OF AUDIT COMMITTEE IN APPROVING AUDIT PLANS

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1. PURPOSE OF REPORT

1.1 To provide Members of the Audit Committee advice regarding their role in approving future audit plans.

2. BACKGROUND

2.1 In order to ensure that the Audit Committee fulfils its requirements in relation to the approval of audit plans, the Better Governance Forum has provided a briefing paper for Audit Committee members in public sector bodies.

2.2 The briefing paper, attached as **Appendix A**, provides background information and questions relevant to the role of Audit Committee members in the process. The briefing paper considers the following areas:

- Why draw up an audit plan?
- Who is involved?
- How is the audit plan produced?
- What does the audit plan cover?
- The audit committee's role,
- When is the audit plan written?

There are also a number of questions posed for members to consider.

3 RECOMMENDATION

3.1 It is recommended that Members review the contents of the briefing paper and consider the issues raised when approving future audit plans.

Appendix A

Introduction

Dear Audit Committee Member,

This is a new briefing paper for audit committee members in public sector bodies. It has been produced by the CIPFA Better Governance Forum and is free to our subscribing organisations. Its aim is to provide members of audit committees with direct access to relevant and topical information that will support them in their role. This first issue includes an article to help you review your internal audit plan and pointers to other information and guidance relevant to your role.

The CIPFA Better Governance Forum is part of the Chartered Institute of Public Finance and Accountancy which is the leading body for setting standards of governance and recommended practice for audit committees in local government and other parts of the public sector. The Forum is a subscription network covering all aspects of governance providing guidance, briefings and workshops. I hope you will find this first issue helpful. It is our intention to produce this briefing three times a year. It will be emailed to the key contact in your organisation who will be able to email it to you or print it if you prefer. If you want to make sure you receive your copy directly please provide us with your details using the link on page 3. We welcome feedback on this issue and suggestions for future topics. Please let us know if we have got this right.

Best wishes
Diana Melville
Governance Advisor
CIPFA Better Governance Forum

Reviewing the Audit Plan

At least once a year, but possibly more frequently, both your internal and external audit teams will ask you to review their audit plans and approve them. If you aren't familiar with audit plans, you may well be asking yourself how to do this and how you can add value. In this article, I will discuss:

- Why draw up an audit plan?
- Who is involved?
- How is the audit plan produced?
- What does the audit plan cover?
- When is the audit plan written?
- Your role in relation to the audit plan.

I will finish with a "dashboard" of key questions for you to ask to satisfy yourself that the plan has been drawn up appropriately and will deliver the assurance that you need as an audit committee member. While I concentrate on your role in relation to internal audit, many of these points also relate to external audit.

Why draw up an audit plan?

An audit plan is needed to ensure that your auditors address all the main areas of risk within your organisation and can provide assurance to support your Annual Governance Statement or Statement on Internal Control. At the end of each year the head of internal audit provides an opinion on the effectiveness of the control environment so it is vital that the plan is sufficient to support that opinion. It is also needed to ensure auditors use their limited resources (budget, time, people and expertise) to best effect. Almost inevitably audit needs outstrip audit resources and the plan will help your audit team set its priorities, in discussion with you.

Who is involved?

The audit plan is normally drawn up by the head of internal audit, in consultation with directors and members of the audit team. As the internal audit plans and external audit plans should be aligned, each should consult the other as part of this process.

How is the audit plan produced?

The audit plan is 'risk-based' to address the financial and non-financial risks faced by your organisation and your key priorities. Your organisation's risk register and the effectiveness of risk management will be reviewed to help develop the plan. The plan may also include work to be undertaken on behalf of your external auditor. The identified audits will be balanced against the resources available and the plan drawn up accordingly.

What does the audit plan cover?

The audit plan should show how your internal audit strategy is going to be achieved in accordance with the section's terms of reference. Plans include a combination of planned work and allowances for reactive work. They are always flexible so that they can reflect the changing risks and priorities within your organisation. Plans will also include allowances for "non-chargeable" time.

Planned audit work consists of a series of reviews of different aspects of your organisation's operations. The plan will include some high risk areas, for example areas of significant financial risk or high profile projects or programmes. Or they could be areas where there are concerns about poor performance, fraud or emerging risks. Some higher risk audits may feature annually in audit plans. Other areas, particularly financial systems, may be audited regularly even if they are well controlled because of their significance to the financial statements. The frequency will usually be agreed with the external auditor. Other parts of the plan will reflect the risks and priorities of the organisation and the judgement of the head of internal audit.

Reactive audit work may include investigations, giving advice, supporting working groups and other such matters. Non-chargeable time includes annual leave, training, administration, team meetings etc. A working year is approximately 260 days. A typical auditor (not a trainee or a manager) will carry out about 200 audit days/year.

When is the audit plan written?

Detailed audit plans normally cover the organisation's financial year, although this is not mandatory. The audit plan is, therefore, generally written a few months before the start of the audit year for approval by the audit committee at the meeting before the start of that year. As the plan has to be flexible, you should be kept informed of minor changes and receive a revised plan for approval if there are any significant changes during the year.

There may also be a strategic plan that outlines the main direction for the audit team over a longer period than a year (perhaps three years). This is particularly useful to understand the wider coverage of risks and controls.

The audit committee's role

The audit committee should be both challenging of the plan and supportive in its delivery. You need to be sure that the organisation's risks and priorities are considered, that the plan is aligned with the audit strategy and terms of reference, that internal and external audit have liaised in drawing up their plans and that your auditors have exercised their independence and have not been unduly influenced by others in deciding what they will or (even more importantly) will not examine. You could review the audit strategy and terms of reference at the same time to ensure that they are still relevant and appropriate.

You also need to consider how the plan relates to other sources of assurance to support the Annual Governance Statement or Statement on Internal Control, for example assurance from the risk management process or management assurances. Taken as a whole, will you get the assurance you need?

Once the plan has been approved, your role is then to monitor activity and outcomes against that plan. Is it being delivered? Is the audit work delivering the expected outcome? You may also need to support your auditors, if they are struggling to get auditee engagement or experience a shortfall in resources. Above all, you are there to get action as a result of audit work.

Key questions to ask:

1. Who did the head of internal audit liaise with in drawing up this plan? Did this include external audit?

2. How does this audit plan link to our risk register and our strategic plans?

3. What audits have you left off this plan and why? When do you plan to carry out this work?

4. How does the audit plan fit with other assurance work? Are there any gaps or is there duplication?

Elizabeth Humphrey
Senior Associate, CIPFA Better Governance Forum

Audit Committee

3 December, 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Chief Finance Officer

Subject: Treasury Management 2011/2012

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1. PURPOSE OF REPORT

1.1 To enable the Audit Committee to consider the proposed Treasury Management Strategy for 2011/2012 prior to the strategy being referred to Council in February 2011.

2. BACKGROUND

2.1 The Local Government Act 2003 requires the Council to 'have regard to' the CIPFA Prudential Code and to set prudential indicators for the next three years to ensure that the Authority's capital investment plans are affordable, prudent and sustainable

2.2 The Act therefore requires the Council to set out its Treasury Management Strategy for borrowing and to prepare an Annual Investment Strategy, which sets out the Authority's policies for managing its investments and for giving priority to the security and liquidity of those investments. The Secretary of State has issued Guidance on Local Government Investments which came into force on 1st April, 2004 and they recommend that all Local Authorities produce an Annual Investment Strategy that is approved by full Council, which is also included in this report.

2.3 Revised editions of the CIPFA Prudential Code and CIPFA Treasury Management Code of Practice were issued in November 2009.

2.4 The main changes arising from the new guidance were process related and made it compulsory to adopt practices that the Authority already had in place. One notable change from previous practice was the requirement to nominate a body to be responsible for ensuring effective scrutiny of the Treasury Management Strategy and policies, before making recommendations to Council. This responsibility has been allocated to the Audit Committee.

2.5 The revised Code increases the responsibility of Members' in this area. Training was provided to Members in October 2010 to enable better scrutiny of the Treasury Management Strategies.

2.6 This report outlines the Authority's Treasury Management Strategy for 2011/2012. This report would normally include details of prudential indicators for 2011/2012 – 2013/2014 however as we are awaiting Government announcements on capital funding we have insufficient information to calculate many of the prudential indicators.

2.7 As the Treasury Management Strategy outlines the key principles covering the operation of the Authority's borrowing and investment strategy the unavailability of this information does not prevent the Audit Committee considering the Treasury Management Strategy. Full details of prudential indicators will be included when this report is referred to Council in February 2011.

2.8 The report also sets out the expected treasury operations for this period. It fulfils key legislative requirements:

- The Treasury Management Strategy Statement which sets out the planned borrowing and investment strategies and the limitations on treasury activity by the use of treasury prudential indicators.

- The Investment Strategy which sets out the Authority's criteria for investment counterparties and limiting exposure to the risk of loss. This strategy is in accordance with the Department of Communities and Local Government (CLG) Investment Guidance.

2.9 The above policies and parameters provide an approved framework within which officers undertake the day to day capital and treasury activities.

2.10 This report covers the following areas:

- Outlook for Interest Rates;
- Capital Financing Requirement and Borrowing Strategy;
- Investment Strategy; and,
- Prudential Indicators and Treasury Limits

3. OUTLOOK FOR INTEREST RATES

3.1 The table below provides the latest interest rate forecasts provided by Butlers.

Annual Average %	Bank Rate	Money Rates		PWLB Rates		
		3 month	1 year	5 year	25 year	50 year
2010/11	0.5	0.7	1.5	2.6	4.6	4.7
2011/12	0.7	1.0	1.8	3.3	5.3	5.4
2012/13	1.7	2.0	2.8	4.2	5.5	5.6
2013/14	3.1	3.2	3.7	4.8	5.6	5.7
2014/15	4.0	4.2	4.5	5.6	5.6	5.8
2015/16	4.0	4.2	4.2	5.3	5.5	5.5

3.2 Short-term rates are expected to remain on hold for a considerable time. The recovery in the economy has commenced and recent growth data has come in at the high side of expectations. However, this growth data needs to be seen in the context of a severe recession and this higher rate is unlikely to be sustained, with growth expected to revert back to more insipid levels. The danger of a double-dip recession is fading but the crisis in the Euro-zone, the prospects of tight economic policies at home and tenuous consumer confidence means the threat has still not evaporated completely.

3.3 The Office for Budget Responsibility has presented a realistically downbeat view of the economy's recovery prospects over the short and medium term, projecting that growth will struggle to exceed its trend rate in the current parliament. The Government's determination to cut the size of the public sector deficit considerably more quickly than its predecessor will be a drag upon activity in the medium term.

3.4 The void left by significant cuts in public spending will have to be filled by a number of alternatives – corporate investment, rising exports and consumer expenditure. In terms of sheer magnitude, the latter is the most important and a strong recovery in this area is by no means certain. The combination of the desire to reduce the level of personal debt and continued job uncertainty is likely to weigh heavily upon spending. This will be amplified by fiscal policy tightening, outlined in the Budget and expanded upon in the 20 October Comprehensive Spending Review. Without a rebound in personal spending, any recovery in the economy is set to be weak and protracted.

3.5 The Bank of England admits that inflation will remain above target until 2012. Inflation performance remains a key risk to the future course of interest rates. Nevertheless, the perceived need to counter the fiscal squeeze via accommodative monetary policy suggests that barring a deterioration from the current situation, the Monetary Policy Committee will be prepared to hold rates at very low levels until the latter stages of 2011.

3.6 The outlook for long-term interest rates is favourable in the near term but is set to deteriorate in the latter part of 2011. Yields will be suppressed by continued investor demand for safe haven instruments following the uncertainties and unfolding tensions within the entire Euro-zone. In addition to this, the market has been underpinned by evidence of decelerating activity in major economies and the coalition government's apparent determination to deal with the parlous state of public sector finances. These two factors will restrict any deterioration in gilt market performance in the near term.

3.7 However, while the UK's fiscal burden will almost certainly ease, it will be a lengthy process and deficits over the next two to three financial years will still require a very heavy programme of gilt issuance. The latest Bank Inflation Report suggests the market will not be able to rely upon Quantitative Easing indefinitely to alleviate this enormous burden.

3.8 Eventually, the absence of the Bank of England as the largest buyer of gilts will shift the balance between supply and demand in the gilt-edged market. Other investors will almost certainly require some incentive to continue buying government paper. This incentive will take the form of higher yields.

4. CAPITAL FINANCING REQUIREMENT AND BORROWING STRATEGY

4.1 The Council's Borrowing Need (the Capital Financing Requirement)

4.2 The Authority's Borrowing Strategy is driven by the Capital Financing Requirement (CFR) and the Authority's view of interest rates. The CFR is simply the total outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Authority's underlying borrowing need and at 31 March 2010 the Authority's CFR was £86.035m. At present it is not possible to calculate the Authority's estimated CFR for the next 3 years but this will be included in the report to Council when the Government has announced capital allocations for 2011/2012 (refer to **Appendix A**, Table 1 & 2).

4.3 The Authority is required to pay off an element of the CFR each year through a revenue charge called the Minimum Revenue Provision (MRP), although it is also allowed to undertake additional voluntary payments (VRP).

4.4 CLG Regulations require the Council to approve **an MRP Statement** in advance of each year. The Council is recommended to approve the following MRP Statement

- For capital expenditure incurred before 1st April, 2008 the Council's MRP policy is to calculate MRP in accordance with former CLG Regulations. This is 4% of the Capital Financing Requirement except where the Council makes Voluntary Revenue Payments for Departmental Prudential Borrowing, which is in excess of the amount required by these regulations, based on asset life.

- From 1st April, 2008 the Council calculates MRP based on asset life for all assets.

4.5 Borrowing Strategy

4.6 In the short term it is proposed that the Authority will maximise the use of its balance sheet resources to finance 'Under Borrowing'. This reduces investment counterparty risk and shelters against the estimated low level of investments returns. The ability to do this is limited by the level of these resources which are temporary in nature.

4.7 The key risk of deferring long term borrowing is that when the Authority does need to borrow it is not at too high a rate. Long-term fixed interest rates are at risk of being higher over the medium term, and short term rates are expected to rise but from a historically exceptionally low level. The Authority needs to ensure that it achieves benefits from those historically low short term rates whilst retaining the flexibility to lock into longer term rates before they rise significantly. In these circumstance not only is the level of interest rate a factor but the speed at which it is changing. If any of the Authority's LOBOs (Lenders Option Borrowers Option loans) are recalled they will need to be refinanced which will also be from internal resources in the first instance (if available) and then temporary loans until the Authority is confident that the timing is right to obtain long term borrowing. The Chief Finance Officer, under delegated powers, will take the most appropriate form of borrowing depending on the prevailing interest rates at the time, taking into account the risks shown in the forecast above.

4.8 Following the Chancellor's announcement of the Spending Review on 20th October, 2010, HM Treasury instructed PWLB to:

i) Increase the interest rate on all <u>new</u> loans to 1% above the Government's cost of borrowing. This change took immediate effect;

ii) Publish at the end of each month a list of individual loans it has made to local authorities, including the type, amount, term and rate applying to each loan.

4.9 HM Treasury has indicated "that the interest rates increase is based on the Government having to make difficult choices around borrowing and capital investment. To ensure that the rate at which loans are made available to local authorities better reflects the availability of capital funding post-spending review and encourages optional borrowing and investment decisions". Interestingly, the increase in PWLB rates will generate a surplus to the Treasury.

4.10 Local authorities will still be able to finance capital expenditure requirements by borrowing monies from banks. However, commercial banks will use PWLB interest rates as a benchmark and increase interest rates accordingly. The increase in PWLB interest rates therefore increases borrowing costs for local authorities at a time of reducing revenue grant funding. In the short term this is manageable owing to short term interest rates. However, in the medium term this change increases risk to the Authority and this position will need to be managed carefully to protect the Authority's longer term financial position.

4.11 HM Treasury have also indicated that publishing details of new PWLB loans is designed to increase transparency of decisions made by local authorities. In my view this is simply another layer of bureaucracy as the prudential code and associated reporting requirements already provide comprehensive arrangements for reporting on treasury management issues.

4.12 This change will also make PWLB debt rescheduling more problematic in the future.

4.13 **Limits to Borrowing Activity**

4.14 Once the CFR has been determined the Authority will need to set the strategy to fund the borrowing requirements. Within the prudential indicators there are a number of key indicators to ensure the Authority operates its activities within well defined limits.

4.15 For the first of these the Authority needs to ensure that its total borrowing net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2011/2012 and the following two financial years . This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

4.16 Table 3 at **Appendix A** shows two key limits for the monitoring of debt in 2010/2011, however it is not possible to set these limits for 2011/2012 until the CFR can be calculated. The Operational Limit is the likely limit the Authority will require and is aligned closely with the actual CFR on the assumption that cash flow is broadly neutral.

4.17 The Authorised Limit for External Debt is a further key prudential indicator to control the overall level of borrowing. This represents a limit beyond which external debt is prohibited, and this limit needs to be set or revised by full Council. In practice it needs to take account of the range of cash flows that might occur for the Authority in addition to the CFR. This also includes the flexibility to enable advance refinancing of existing loans.

4.18 The Chief Finance Officer reports that the Authority complied with these prudential indicators in the current year and does not envisage difficulties for the future.

4.19 The Authority has some flexibility to borrow funds this year for use in future years. The Chief Finance Officer may do this under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Whilst the Chief Finance Officer will adopt a cautious approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme or to fund future debt maturities. Any borrowing in advance of need will be reported to the Council in the next treasury management report.

5. INVESTMENT STRATEGY

5.1 The primary objectives of the Authority's investment strategy in order of importance are:

- safeguarding the re-payment of the principal and interest of its investments on time;
- ensuring adequate liquidity;
- investment return.

5.2 Following the economic background above, the current investment climate has one over-riding risk consideration which is that of **counterparty security risk**. As a result of these underlying concerns officers are implementing an operational investment strategy which tightens the controls already in place in the approved investment strategy.

5.3 **Benchmarking**

5.4 A development in the revised Codes and the CLG consultation paper is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Security and liquidity benchmarks are new requirements to the Member reporting and benchmarks in these areas are significantly less developed. The application of these is also more subjective in nature.

5.5 These benchmarks are simple targets (not limits) and so may be breached from time to time, depending on movements in interest rates and counterparty criteria. The purpose of the benchmark is to assist monitoring and illuminate any changes to the strategy. Any breach of the benchmarks will be reported, with supporting reasons in the Mid-Year or Annual Report.

5.6 The benchmark for monitoring security is based on the historical risk of default associated with the credit rating of an organisation. The higher rated counterparties have a lower rate of historic default.

5.7 The Table below sets out the historic default percentages for each type of credit rated institution and the period of deposit.

	Maturity Period				
Years	**1**	**2**	**3**	**4**	**5**
AAA	0.00%	0.01%	0.05%	0.10%	0.17%
AA	0.03%	0.06%	0.08%	0.14%	0.20%
A	0.08%	0.22%	0.37%	0.52%	0.70%
BBB	0.24%	0.68%	1.19%	1.79%	2.42%
BB	1.22%	3.24%	5.34%	7.31%	9.14%
B	4.06%	8.82%	12.72%	16.25%	19.16%
CCC	24.03%	31.91%	37.73%	41.54%	45.22%

5.8 The Authority will aim to ensure that the historic default probability of its investment portfolio will not exceed 0.2%.

5.9 An additional proposed benchmark is the average risk of default. This is based on the historic risk of default multiplied by the value of each investment. It does not constitute the actual expectation of loss. Rather it is intended to give a guide as to the relative security of investments. For the forthcoming year this is expected not to exceed £100,000.

5.10 To ensure adequate Liquidity the Authority seeks to maintain a bank overdraft of £1.5m. In addition the Authority will make use of call accounts to enable cash to be obtained with immediate notice. The proposed benchmark for monitoring liquidity is 'Weighted Average Life'. This reflects the average number of days to maturity for investments and therefore gives an indication of the liquidity profile of investments held. For the forthcoming year because of the lack of value obtainable for deposits exceeding 12 months and the need to ensure maximum security this benchmark is expected to be 0.5 years, with a maximum of 3 years.

5.11 **Investment Counterparty Selection Criteria**

5.12 The Authority's criteria for providing a pool of high quality investment counterparties is as follows:

- **Banks** – the Authority will use UK banks which have at least the following Fitch (or Moody's and Standard and Poors equivalent) ratings (where rated):

  - Short Term: F1
  - Long Term: A-
  - Individual / Financial Strength: C (Fitch / Moody's only)
  - Support: 3 (Fitch only)

- **Building Societies** – the Authority will invest with building societies where they have asset base of more than £1bn and form part of the HM Treasury Guarantee scheme, or where societies meet the ratings for banks outlined above. These are currently excluded from the operational counterparty list as a result of reduced credit ratings in the sector generally but are included in the Authority's criteria on the basis that they may be reinstated if ratings improve.

- **Other Local Authorities**.

- **Debt Management Office –** this is a UK Government Agency which manages debt on behalf of the Government.

5.13 The rating criteria uses the **lowest common denominator** method of selecting counterparties and applying limits. This means that the application of the Authority's minimum criteria will apply to the lowest available rating for any institution. For instance if an institution is rated by two agencies, one meets the Authority's criteria, the other does not, the institution will fall outside the lending criteria. This is in compliance with a CIPFA Treasury Management Panel recommendation in March, 2009 and the CIPFA Treasury Management Code of Practice.

5.14 Credit rating information is supplied by our treasury consultants on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered on a daily basis before investments are made. For instance a negative rating watch applying to a counterparty at the minimum Authority criteria will be suspended from use, with all others being reviewed in light of market conditions.

5.15 Note that the above criteria only includes UK institutions and therefore has never included Icelandic banks, owing to the risk that if these banks ran into financial difficulties the Icelandic Government may not have been able to underwrite depositors funds.

5.16 The criteria is different to that used to define Specified and Non-Specified investments which is the classification used by CLG regulations. This is because it is intended to create a pool of high quality counterparties for the Authority to use rather than defining what its investments are. Further details of the Specified/Non Specified criteria are contained at **Appendix B**.

5.17 From February 2009 the Council 'pooled' its investments with Cleveland Fire Authority to help spread counterparty risk. As a result of this collaboration both organisations shared the same Treasury Management Strategies and criteria determining approved investment counter-parties. During 2010/2011 it became necessary to unwind this 'pooled' fund as the investment and borrowing needs of two authorities now differ. The Chief Finance Officer, using delegated powers, has revised the individual counterparty limits for the Council in order to assist the unwinding of the fund.

5.18 The table below shows the revised limits proposed for the Council:

	Fitch	Moody's	Standard & Poors	Counterparty Limit	Time Limit
Upper Limit Category	F1+/AA-	P-1/Aa3	A-1+/AA-	£7.5m	3 years
Middle Limit Category	F1/A-	P-1/A3	A-1/A-	£1.75m	364 days
Lower Limit Category	Unrated bank subsidiaries and building societies with assets over £1bn			£1.5m	6 months
Other Limits	Other Local Authorities			No Limit	3 years
	Nationalised Banks			£7.5m	3 years
	Debt Management Office			£15m	3 years
	UK Banks covered by UK Government Guarantee			£7.5m	3 years

5.19 The above limits set the overall framework for investment. In practice the Chief Finance Officer uses his delegated powers to set operational limits which further tighten the lending criteria as necessary in response to developments caused by the Global 'credit crunch'. These actions reflect the Chief Finance Officer's assessment of risk which is particularly important as credit ratings are not a guarantee of an organisation's financial strength and can only provide a starting point for assessing risk. This flexibility is needed to take advantage of opportunities arising where maximum security can be obtained to reduce the risk of financial loss, while still benefitting from competitive rates of return.

5.20 In the normal course of the Authority's cash flow operations it is expected that both Specified and Non-specified investments will be utilised for the control of liquidity as both categories allow for short term investments.

5.21 The use of longer term instruments (greater than one year from inception to repayment) will fall in the Non-specified investment category. These instruments will only be used where the Authority's liquidity requirements are safeguarded. This will also be limited by the longer term investment limits.

5.22 **Economic Investment Considerations**

5.23 Expectations on shorter-term interest rates, on which investment decisions are based, show the likelihood of the current 0.5% Bank Rate remaining flat but with the possibility of a rise in mid-2011. The Authority's investment decisions are based on comparisons between the rises priced into market rates against the Authority's and advisers own forecasts.

5.24 There is an operational difficulty arising from the current economic climate. There is currently little value investing longer term whilst credit quality is uncertain/reduced. Whilst some selective options do provide additional yield uncertainty over counterparty creditworthiness suggests shorter term investments would provide better security.

5.25 The criteria for choosing counterparties set out above provides a sound approach to investment in “normal” market circumstances. Whilst Members are asked to approve the base criteria above, under the exceptional current market conditions the Chief Finance Officer may temporarily restrict further investment activity to those counterparties considered of higher credit quality than the minimum criteria set out for approval. These restrictions will remain in place until the banking system returns to “normal” conditions. Similarly the time periods for investments will be restricted.

5.26 Following the increased risk and uncertainty arising from the unprecedented recent economic crisis the Chief Finance Officer has continued to adopt an even more vigilant approach resulting in what is effectively a ‘named’ list. This consists of a very select number of counterparties that are considered to be the lowest risk. This has involved the Council temporarily suspending making new deposits with all building societies except the Nationwide, which has a financial standing rating equivalent to the major clearing banks.

5.27 The Council’s approach of suspending building societies from the counterparty list has proven prudent as the ratings for all building societies (except Nationwide) have recently been downgraded owing to continuing concerns about their financial stability and exposure to property loans.

5.28 The Council has also continued to exclude all foreign banks, including Irish banks from the list following the downgrading of the countries sovereign rating.

5.29 At the time of writing this report there was ongoing speculation about the solvency of Ireland and whether a European Union bail-out would be necessary. This position could potentially affect other European countries and in particular the so called “PIGS” countries (Portugal, Italy, Greece & Spain). It also continues to undermine confidence in Irish banks.

5.30 Examples of these restrictions would be the greater use of the Debt Management Deposit Account Facility (DMADF – a Government body which accepts local Authority deposits), Money Market Funds, guaranteed deposit facilities and strongly rated institutions offered support by the UK Government. The credit criteria have been amended to reflect these facilities.

5.31 **Sensitivity to Interest Rate Movements**

5.32 The Authority will be required to disclose in its Statement of Accounts the impact of risks on the Authority’s treasury management activity. Whilst most of the risks facing the treasury management service are addressed elsewhere in this report (credit risk, liquidity risk, market risk, maturity profile risk), the impact of interest rate risk is discussed but not quantified. Once details of capital allocations are received from Government this will be quantified. Table 4 shown in **Appendix A** will highlight the estimated impact of a 1% increase/decrease in all interest rates to the estimated treasury management costs/income for next year. That element of the debt and investment portfolios which are of a longer term, fixed interest rate nature will not be affected by short interest rate changes.

5.33 **Treasury Management Limits on Activity**

5.34 There are four further treasury activity limits and the purpose of these are to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs/improve performance.

5.35 The limits are:

i) Upper limits on variable interest rate exposure – This identifies a maximum limit for variable interest rates based upon the debt position net of investments.

ii) Upper limits on fixed interest rate exposure – Similar to the previous indicator this covers a maximum limit on fixed interest rates.

iii) Maturity structure of borrowing.

iv) Maximum principal sums invested.

5.36 The proposed limits for (i) and (ii) cannot be set until we are able to calculate the CFR (Table 5, **Appendix A**).

5.37 Limits for the 'Maturity Structure of Borrowing' are intended to reduce exposure to large fixed rate sums falling due for refinancing. The view of the Chief Finance Officer is that limits on fixed and variable rates for **borrowing** are unhelpful and could lead to unnecessary higher costs of borrowing. Previous experience has shown that it is possible to move from a position of predominantly fixed rate borrowing to variable rate borrowing and then back to fixed rate borrowing over a period of two years. Currently the market is so volatile that the Authority should ensure maximum flexibility to minimise costs to the revenue budget in the medium term. These limits cannot be set until the estimated CFR can be calculated (Table 6**, Appendix A**).

5.38 The limits in Tables 5 & 6, when set, will therefore allow for borrowing up to the Capital Financing Requirement at either variable or fixed rates. The intention is to move to fixed rate borrowing when rates are at an appropriate level and may require the temporary use of variable rate borrowing in the interim.

5.39 Total principal funds invested for greater than 364 days – These limits are set with regard to the Authority's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

Limit for Maximum Pincipal Sums Invested > 364 days			
	1 year £000	**2 years £000**	**3 years £000**
Maximum	30,000	20,000	15,000

5.40 **Performance Indicators**

5.41 The Code of Practice on Treasury Management requires the Council to set performance indicators to assess the adequacy of the treasury function over the year. These are distinct historic indicators, as opposed to the prudential indicators, which are predominantly forward looking. The Authority will produce the following performance indicators for information and explanation of previous treasury activity:

- Average rate of borrowing for the year compared to average available
- Debt – Average rate movement year on year
- Investments – returns above the 7 day LIBID rate

5.42 **Treasury Management Advisers**

5.43 The Authority uses Butlers as its treasury management consultants (Butlers have recently been taken over by Sector). The company provides a range of services which include:

- Technical support on treasury matters, capital finance issues and the drafting of Member reports;
- Economic and interest rate analysis;
- Debt services which includes advice on the timing of borrowing;
- Debt rescheduling advice surrounding the existing portfolio;
- Generic investment advice on interest rates, timing and investment instruments;
- Credit ratings/market information service comprising the three main credit rating agencies;

5.44 Whilst the advisers provide support to the internal treasury function, under current market rules and the CIPFA Code of Practice the final decision on treasury matters remains with the Authority. This service is subject to regular review.

6.0 PRUDENTIAL INDICATORS AND TREASURY LIMITS

6.1 As indicated earlier in the report the CIPFA Prudential Code requires the Council to set prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity, and reflects the outcome of the Authority's underlying capital appraisal systems. At the time of preparing this report it is not possible to calculate many of the indicators as the government has not yet provided detailed capital allocations for the next three years. These will be reported to full Council with the Medium Term Financial Strategy.

6.2 **Appendix A** shows the prudential indicators that will be included in the report to Council and for Members information include the 2010/2011 indicators. Details of the key indicators are set out in the following paragraphs.

6.3 **CIPFA Treasury Management Code of Practice**

6.4 The first prudential indicator is confirmation that the Authority has adopted the CIPFA Treasury Management Code of Practice.

6.5 **Capital Expenditure**

6.6 A certain level of capital expenditure is supported by the Government through the revenue grant system. For 2011/12 the Government has not yet provided a supported borrowing allocation. Any decisions to spend above the supported borrowing allocation will be classified as unsupported capital expenditure and the Council needs to have regard to the following when approving such proposals:

- Service objectives (e.g. strategic planning);
- Stewardship of assets (e.g. asset management planning);
- Value for money (e.g. option appraisal);
- Prudence and sustainability (e.g. implications for external borrowing and whole life costing);
- Affordability (e.g. implications for the Council Tax);
- Practicality (e.g. the achievability of the forward plan).

6.7 The revenue consequences of capital expenditure, particularly the unsupported capital expenditure, will need to be paid for from the Authority's own resources.

6.8 Capital expenditure can be funded for immediately by applying capital resources such as capital grants or revenue resources, but if these resources are insufficient any residual capital expenditure will add to the Authority's borrowing requirement.

6.10 **Affordability Prudential Indicators**

6.11 These indicators are intended to give an indication of the affordability of the planned capital expenditure financed by borrowing. **Appendix A** details affordability prudential indicators.

7. RECOMMENDATIONS

7.1 It is recommended that Members:

i) Consider and approve the proposed Treasury Management Strategy detailed in the report prior to the Strategy being referred to Council in February 2011.

ii) Note that a number of technical prudential indicators will be calculated once the Government announces capital allocations, and this will be reported to Council in February 2011.

Appendix A

Prudential Indicators to be reported to Full Council

Table 1 – Capital Expenditure

Capital Expenditure	2010/11 Original £'000	2010/11 Revised £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Capital Expenditure	34,167	52,039	TBD	TBD	TBD
Financed by:			TBD	TBD	TBD
Capital grants and contributions	20,559	38,580	TBD	TBD	TBD
Capital Receipts	0	257	TBD	TBD	TBD
Revenue	0	0	TBD	TBD	TBD
Net financing need for the year	**13,608**	**13,459**	**TBD**	**TBD**	**TBD**

Table 2 – Capital Financing Requirement

	2010/11 Original £'000	2010/11 Revised £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
CFR b/f	92,829	86,035	TBD	TBD	TBD
Capital Expenditure Financed by Borrowing	13,608	13,459	TBD	TBD	TBD
Less MRP/VRP and other financing movements	4,476	4,147	TBD	TBD	TBD
CFR c/f	**101,960**	**95,347**	**TBD**	**TBD**	**TBD**

Table 3 – Limits on Borrowing Activity

Borrowing Limits	2010/11 Revised £'000	2011/12 Estimate £'000	2012/13 Estimate £'000	2013/14 Estimate £'000
Operational Limit	102,000	TBD	TBD	TBD
Authorised limit	115,000	TBD	TBD	TBD

Table 4 – Sensitivity to Interest Rates

£m	2011/12 Estimated + 1%	2011/12 Estimated - 1%
Revenue Budgets	TBD	TBD
Interest on Borrowing	TBD	TBD
Net General Fund Borrowing Cost	TBD	TBD
Investment income	TBD	TBD

TBD – To Be Determined

Table 5 – Interest Rate Exposure Limits

Interest rate Exposures	2010/11 £000 Upper	2011/12 £000 Upper	2012/13 £000 Upper
Limits on fixed interest rates:			
• Debt	102,000	TBD	TBD
• Investments	(30,000)	TBD	TBD
Limits on fixed interest rates based on net debt	72,000	**TBD**	**TBD**
Limits on variable interest rates			
• Debt	102,000	TBD	TBD
• Investments	(60,000)	TBD	TBD
Limits on variable interest rates based on net debt	42,000	**TBD**	**TBD**

Table 6 – Maturity Structure of Fixed Interest Rate Borrowing

Maturity Structure of fixed interest rate borrowing 2011/12				
	2010/11 £000 Lower Limit	2010/11 £000 Upper Limit	2011/12 £000 Lower Limit	2011/12 £000 Upper Limit
Under 12 months	0	93,000	TBD	TBD
12 months to 2 years	0	102,000	TBD	TBD
2 years to 5 years	0	102,000	TBD	TBD
5 years to 10 years	0	102,000	TBD	TBD
10 years to 20 years	0	102,000	TBD	TBD
20 years to 30 years	0	102,000	TBD	TBD
30 years to 40 years	0	102,000	TBD	TBD
40 years to 50 years	0	102,000	TBD	TBD
50 years to 60 years	0	102,000	TBD	TBD
60 years to 70 years	0	102,000	TBD	TBD

Affordability Prudential Indicators

Table 7 – Incremental Impact of Capital Expenditure on Council Tax

This indicator identifies the revenue costs associated with new schemes introduced to the three year Capital Programme recommended in the budget strategy report compared to the Authority's existing approved commitments and current plans

%	2010/11 Estimate	2011/12 Estimate	2012/13 Estimate	2013/14 Estimate
Ratio	7.32%	TBD	TBD	TBD

TBD – To Be Determined

Table 8 – Ratio of Financing Costs to Net Revenue Stream

This shows the net cost of capital borrowing as a percentage of the net budget, which is spent on servicing debt. The upwards trend reflects the increasing costs associated with each year's capital expenditure and the expected reduction in investment income.

	Forward Projection 2010/11 £'000	Forward Projection 2011/12 £'000	Forward Projection 2012/13 £'000	Forward Projection 2013/14 £'000
CouncilTax - Band D	£4.62	TBD	TBD	TBD

TBD – To Be Determined

Appendix B

Credit And Counterparty Risk Management

The CLG issued Investment Guidance in 2010, and this forms the structure of the Council's policy below.

The key intention of the Guidance is to maintain the current requirement for authorities to invest prudently and that priority is given to security and liquidity before interest return. In order to facilitate this objective the guidance requires this Council to have regard to the CIPFA publication Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. This Council has adopted the Code and applies its principles to all investment activity. In accordance with the Code, the Chief Finance Officer has produced its treasury management practices covering investment counterparty policy which requires approval each year.

Annual Investment Strategy - The key requirements of both the Code and the investment guidance are to set an annual investment strategy, as part of its annual treasury strategy for the following year, covering the identification and approval of following:

- The strategy guidelines for decision making on investments, particularly non-specified investments.
- The principles to be used to determine the maximum periods for which funds can be committed.
- Specified investments the Council will use. These are high security (i.e. high credit rating, although this is defined by the Council, and no guidelines are given), and high liquidity investments in sterling and with a maturity of no more than a year.
- Non-specified investments, clarifying the greater risk implications, identifying the general types of investment that may be used and a limit to the overall amount of various categories that can be held at any time.

The strategy proposed for approval by Members is set out below.

Strategy Guidelines – The main strategy guidelines are contained in the body of the Treasury Strategy Statement.

Specified Investments – These investments are sterling investments of not more than one-year maturity, or those which could be for a longer period but where the Council has the right to be repaid within twelve months if it wishes. These are low risk assets where the possibility of loss of principal or investment income is small. These would include investments with:

1. The UK Government (such as the Debt Management Office, UK Treasury Bills or a Gilt with less than one year to maturity).

2. Other Councils.

3. Pooled investment vehicles (such as money market funds) that have been awarded a high credit rating by a credit rating agency. This covers pooled investment vehicles, such as money market funds, rated AAA by Standard and Poor's, Moody's or Fitch rating agencies.

4. A body that has been awarded a high credit rating by a credit rating agency (such as a bank or building society. This covers bodies with a minimum rating of A- (or the equivalent) as rated by Standard and Poor's, Moody's or Fitch rating agencies. Within these bodies, and in accordance with the Code, the Council has set additional criteria to set the time and amount of monies which will be invested in these bodies. This criteria is:

	Fitch	Moody's	Standard & Poors	Limit for Investment Fund	Time Limit
Upper Limit Category	F1+/AA-	P-1/Aa3	A-1+/AA-	£10m	364 days
Middle Limit Category	F1/A-	P-1/A3	A-1/A-	£7m	364 days
Other Institution Limits	Other Local Authorities			No Limit	364 days
	Nationalised Banks			£10m	364 days
	Debt Management Office			£20m	364 days
	UK Banks covered by UK Government			£10m	364 days

Non-Specified Investments – Non-specified investments are any other type of investment (i.e. not defined as Specified above). The identification and rationale supporting the selection of these other investments and the maximum limits to be applied are set out below. Non specified investments would include any investments with:

- **Building societies not meeting the basic security requirements under the specified investments**. The operation of some building societies does not require a credit rating, although in every other respect the security of the society would match similarly sized societies with ratings. The Investment Fund may use building societies with assets over £1bn. These will be limited to £2.5m over 3 months.
- Any **bank or building society** that has a minimum long term credit rating of A- for deposits with a maturity of greater than one year (including forward deals in excess of one year from inception to repayment).

	Fitch	Moody's	Standard & Poors	Money Limit	Time Limit
Upper Limit Category	F1+/AA-	P-1/Aa3	A-1+/AA-	£10m	3 years
Other Local Authorities				No limit	3 years
Nationalised Banks				£7m	3 years
Building Societies				£2m	
Debt Management Office				£20m	3 years
UK Banks covered by UK Government				£7m	3 years

The Monitoring of Investment Counterparties - The credit rating of counterparties will be monitored regularly. The Council receives credit rating advice from its advisers, Butlers, on a daily basis, and as and when ratings change, and counterparties are checked promptly. On occasion ratings may be downgraded when an investment has already been made. The criteria used are such that a minor downgrading should not affect the full receipt of the principal and interest. Any counterparty failing to meet the criteria will be removed from the list immediately by the Chief Finance Officer and if required new counterparties which meet the criteria will be added to the list.

AUDIT COMMITTEE

3 December, 2010

HARTLEPOOL BOROUGH COUNCIL

Report of: Chief Finance Officer

Subject: International Financial Reporting Standards (IFRS) –Update

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1. PURPOSE OF REPORT

1.1. The purpose of this report is to advise Members on the progress being made on the implementation of IFRS.

2. BACKGROUND

2.1. It is a statutory requirement for all local authority's financial statements to be IFRS compliant by 2010/2011. To comply with this requirement the Council will need to revise its accounting policies, change the format of its financial statements and include a significant number of additional disclosures from 2010/2011. In addition, the 2009/2010 comparative figures will need to be restated to comply with IFRS requirements.

2.2. An updated Action Plan **(Appendix 1)** has been produced to ensure the Council complies with the relevant timescales.

3. DETAILED IFRS CHANGES

3.1. The Council identified the following main areas that needed to be addressed to enable the production of IFRS compliant accountings statements. These are detailed in the following paragraphs.

3.2. Employee Benefits

3.3. Under current accounting requirements Local Authorities have not had to make financial accruals at the year end for untaken annual leave entitlement which is being carried forward to the following year. In accordance with IFRS, Local Authorities will either recognise an annual leave accrual or will perform sufficient analysis in this area to satisfy the Auditors that it is not a material amount. Where an accrual is required it has been confirmed that this will be reversed out for tax setting purposes.

3.4. An initial assessment of this area had been undertaken and it was anticipated that the Council would not need to make accruals.

However, CIPFA have now published a model deemed as best practice on the calculation of Teachers Holiday accruals. An assessment of the new guidance indicated that this will produce a material figure which will need to be included in the restated accounts. Further work is still required and the methodology for estimating this amount needs to be agreed with the Council's external auditors.

3.5. Leases

3.6. With the implementation of IFRS the Council is required to separately account for leases of land and buildings.

3.7. A comprehensive review of all of the Council's leases above the de-minimis threshold of £10,000 has been carried out. This exercise ensured that all leases are accounted for correctly under the new regulations. Where the lease was deemed to be a finance lease under the new regulations this will be accounted for on the Council's Balance Sheet. This approach has been agreed with the Council's external auditors.

4. FIXED ASSET ACCOUNTING

4.1. Valuation of Fixed Assets

4.2. IFRS provides clarification regarding valuation methods to be applied, as set out below:

- Operational Land and Buildings are to be held at Fair Value or Depreciated Replacement Cost (DRC) where no fair value exists;
- Investment Properties are to be held at fair value:
- Infrastructure Assets and Community Assets to be held at historical cost;
- Vehicles, Plant and Equipment to be held at fair value;
- Assets that are surplus to requirement are to be held at Lower of Fair Value less costs to sell and carrying amount.

4.3. An initial assessment of this area has clarified that the Council holds the majority of its assets using the correct valuation method. Work is currently being carried out in conjunction with the Council's Estates Section to address those assets which require revaluing.

4.4. Component Accounting

4.5. IFRS introduces the concept of accounting for different components of assets separately, including recognising the asset lives and depreciation charges of each component separately, i.e. a school could be split between buildings with an asset life of forty years and a boiler with an asset life of fifteen years.

4.6. During financial year 2009/10 the Estates Section began to re-value the Council's assets into their components based on existing guidance. This work needed to commence owing to the volume of assets and the tight timescale involved. To date approximately 95% of the assets are already valued under the new component accounting regulations.

4.7. However, as final guidance has not been issued further work maybe required.

4.8. Assets Held for Sale

4.9. The Council is required to review the classification of its fixed assets to ensure that assets held for sale are recognised appropriately in the accounts. Fixed asset disposals in 2009/2010 will be accounted for under existing accounting requirements in the 2009/2010 financial statements. In the 2010/2011 accounts these transactions will need to be restated and accounted for under IFRS requirement. This work is currently being reviewed by officers.

4.10. Infrastructure Assets

4.11. Under IFRS the Council will have to significantly amend the way it accounts for infrastucture assets i.e. roads, footpaths and street lighting. The Department of Transport has indicated that these accounting requirements will not be introduced until 2011/2012 with a 'dry run' in 2010/2011.

4.12. The current method for inclusion in the financial statements is using historical cost. IFRS requires that the Council calculates the Gross Replacement Cost (GRC) and the Depreciated Replacement Cost (DRC). This will provide the Gross Book Value (GBV) and the Net Book Value (NBV) respectively for the accounts; GRC is calculated by multiplying road length by width by the cost per square meter of road. Work is ongoing in conjunction with the Council's Engineers to ensure that the Council comply with this requirement.

5. CONCLUSION

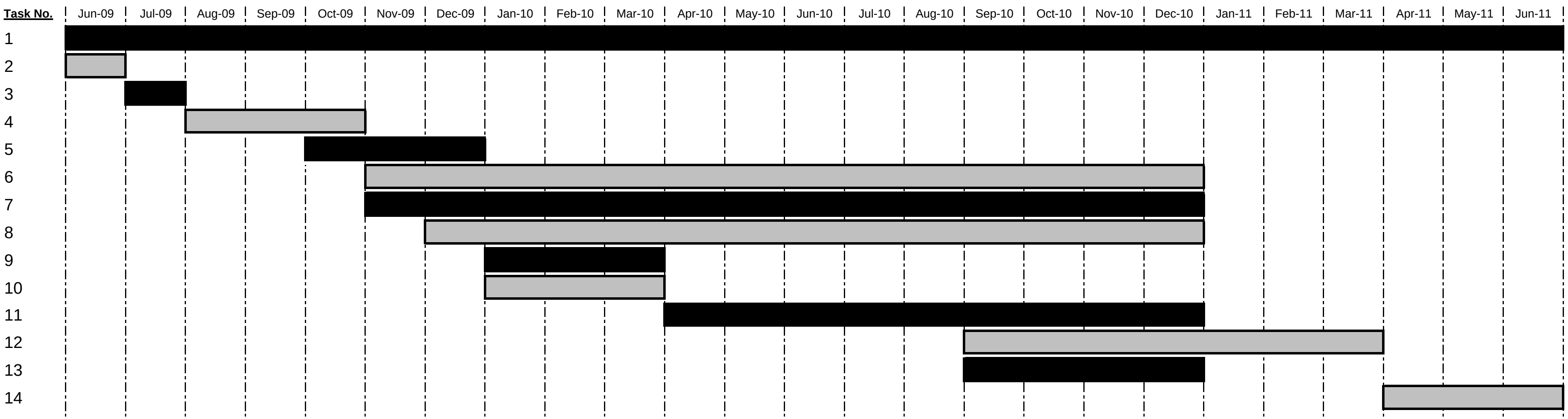
5.1. Work is progressing to ensure that the Accounts are IFRS compliant. It is anticipate that a restated set of accounts for 2009/10 will be produced and audited by the external auditors by the end of this calendar year.

6. RECOMMENDATIONS

6.1. It is recommended that Members note the report.

4.8 Appendix A

IFRS Implementation Plan



Task No.	Task Details	Start Date	End Date	Completed
1	Key staff trained on IFRS Transition (this is an ongoing task where training will be necessary as IFRS requirements are refined)	Jun-09	Jun-11	Ongoing
2	Carry out high level impact assessment using information on CIPFA website (and other resources available)	Jun-09	Jun-09	Jun-09
3	Co-opt key staff onto project team, allocate responsibilities and develop detailed project plan	Jul-09	Jul-09	Jul-09
4	Identify information (e.g. Leases, Tangible Assets and Employee Benefits) required to restate 1 April 2009 balance sheet and 2009/10 Accounts	Aug-09	Oct-09	Oct-09
5	Obtain information (e.g. Leases, Tangible Assets and Employee Benefits) required to restate 1 April 2009 balance sheet and 2009/10 Accounts	Oct-09	Dec-09	May-10
6	Identify changes to accounting policies	Nov-09	Dec-10	
7	Restate 1 April 2009 Balance Sheet balance sheet (including reconciliations between UK GAAP and IFRS)	Nov-09	Dec-10	
8	Identify systems and procedural changes	Dec-09	Dec-10	
9	Identify likely impact on budget	Jan-10	Mar-10	Mar-10
10	Implement systems and procedural changes	Jan-10	Mar-10	Mar-10
11	Testing of systems and procedural changes	Apr-10	Dec-10	
12	Deliver training for Members	Sep-10	Mar-11	
13	Restate 2009/10 accounts in parallel with main 2009/10 accounts process (including reconciliations between UK GAAP and IFRS)	Sep-10	Dec-10	
14	Produce 2010/11 accounts on IFRS basis	Apr-11	Jun-11	