



AUDIT AND STANDARDS COMMITTEE

11 December 2017

Minutes of the Audit and Standards Committee held at the Town Hall, Bexhill-on-Sea on Monday 11 December 2017 at 6:30pm.

Committee Members present: M. Mooney (Chairman), J. Barnes, K.P. Dixon, S.H. Earl and T.W. Graham.

Parish/Town Council Representatives: Councillors Mrs W.M. Miers and T.A. Stainsby (Part A Only).

Advisory Officers present: Executive Director of Resources, Service Manager – Finance and Welfare, Service Manager - Corporate and Human Resources, Financial Services Manager, Customer Services Manager (in part), Audit Manager and Democratic Services Manager.

Also present: Leigh Lloyd-Thomas, Partner, BDO.

AS17/27. MINUTES

The Chairman was authorised to sign the minutes of the meeting of the Audit and Standards Committee held on 26 September 2017 as a correct record of the proceedings.

AS17/28. APOLOGIES

Apologies for absence had been received from Councillors A.K. Azad, R.K. Bird and R.C. Carroll and Independent Members Susan Fellows, Jan Gray and Robert Tye.

AS17/29. EXCLUSION OF PRESS AND PUBLIC

RESOLVED: That the press and public be excluded whilst matters containing exempt information, as prescribed by Part 1 of Schedule 12A of the Local Government Act 1972, as amended and relating to Minute AS17/32 was under consideration. The Appendix submitted in connection with this item and which contains information exempt from publication by virtue of Part 1 of Schedule 12A to the Act shall remain confidential if and so long as, in all the circumstances of the case, the public interest in maintaining the exemption outweighs the public interest in disclosing the information.

PART A STANDARDS REPORTS

PART II DECISIONS TAKEN UNDER DELEGATED POWERS

AS17/30.
(5.1)

CODE OF CONDUCT COMPLAINTS MONITORING

The Committee received the routine report of the Monitoring Officer (MO) which advised that no Code of Conduct complaints had been received since the last meeting and that relatively very few informal issues had been raised during the period.

It was advised that the complainant in respect of a previous complaint (C16-04) had complained to the Local Government Ombudsman (LGO) over the Council's handling of the Standards complaint. The LGO had found no fault in the way that the Council had investigated the complaint, also reported separately at this meeting (see Minute AS17/31 below).

RESOLVED: That the report be noted.

AS17/31.
(5.2)

OMBUDSMAN COMPLAINTS MONITORING AND ANNUAL REVIEW 2016/17

Members considered the report of the Executive Director of Resources that set out details of 13 complaints made to the Local Government Ombudsman (LGO). The Customer Services Manager reported that of the 13 complaints detailed, two were still under investigation and the final decision was awaited in one case; the outcome of these three cases would be reported at the next meeting (June 2018).

Three other cases that had been reported at the last meeting as still being under investigation (homelessness, planning and Standards Investigation processes), had resulted in no fault found in two cases (planning and Standards Investigation processes) and a final decision was awaited with regard to the homelessness case. The additional 10 cases spanned a number of Council services including homelessness services, planning, byelaws, payment methods for garden waste and consultation methods. The Ombudsman had determined that in six cases it would not investigate; in one case it was unable to investigate as it was a legislative matter (byelaws); in one case, fault had been found on part of the Council but no injustice had been caused to the complainant and two cases were still under investigation.

It was noted that whilst Members received performance data on the number of internal complaints received by the Council, through regular performance reports to the Overview and Scrutiny Committee, there was no detail of the subject matter of each complaint, as reported to this Committee for the complaints that had gone on to the LGO. Members were advised that all complaints were handled through the Customer Services Team and monitored by Service Managers / SMT to ensure that lessons were learnt to improve performance and to avoid repeat complaints. The Executive Director of Resources agreed to consider whether more detailed information regarding the nature of the internal complaints could be published for Members' information within the Members' Bulletin, which may help Members in assisting constituents with queries / complaints.

With regard to the Annual Review, it was noted that the number of complaints against the Council still remained relatively low, with 15 recorded (one more than last year's figure of 14 complaints), none of these were upheld, one was partially upheld, two were not upheld and twelve were closed after initial enquires.

RESOLVED: That

- 1) the report be noted; and
- 2) the Executive Director of Resources investigate and consider whether more detailed information regarding the nature of internal complaints could be published for Members' information within the Members' Bulletin.

PART B AUDIT REPORTS

PART I RECOMMENDATIONS TO COUNCIL

AS17/32. TREASURY MANAGEMENT MID-YEAR REVIEW
(7.2)

Cabinet had approved the Council's 2017/18 Treasury Management Strategy Statement in February of this year and the report before Members provided an update.

Full Council was due to consider a Property Investment Strategy on the 18 December 2017 and, if approved, an initial transfer of £7m from cash reserves to property related investments would be made. It was noted that this investment did not preclude the Council from investing other money across the district for regeneration and other purposes. Investing money in property, potentially outside the district, would generate cash for the Council's budget to help offset the impact of declining Government funding. Members were also keen for the Council to consider investing in housing within the district to help with the housing crisis; this would be considered by the recently formed Housing Issues Task and Finish Group.

It was noted that whilst there was uncertainty at present, due the Government and CIPFA currently reviewing the Treasury Management Code of Practice and the Prudential Code, the existing investment strategy would struggle to meet the Council's future income aspirations. Therefore whilst the demands being placed on the Treasury Management Strategy would increase during this period of instability and declining returns from the Council's existing portfolio, the future strategy would need to maintain its focus on prudent management with regard to security and liquidity and the predictability of returns.

As a result of the proposed Property Investment Strategy, it was necessary to make changes to the Treasury Management Strategy Statement for 2017/18 to include property purchases; the changes were detailed at Appendix 3 to the report. In addition, a further amendment was proposed to the limit on non-specified investment category property funds to read "officers in consultation with the

Council's treasury advisers". It was noted that this would now require full Council approval and would be submitted to the meeting on the 18 December.

The Chief Finance Officer's comments on the level of risk with regard to the proposed alternative investment strategies, including property investment were set out within paragraphs 11-15 of the report, and summarised as follows:

- Legal advice sought on the legal powers the Council could rely on to make such investments was shown at Confidential Appendix 5 to the report.
- The Council had been developing alternative investment strategies and was looking to invest a significant proportion of its cash and balances in property assets that had the potential to outperform the Council's current investments.
- The advice showed for this initial investment that reliance could be placed upon the investment powers in Section 12 of the Local Government Act 2003. These powers allowed local authorities to invest both for treasury management purposes (including investment of Council funds) and for any purpose relevant to their functions. As a treasury activity, these investments would be treated as a financial instrument for accounting purposes.
- Assuming reliance was placed on Section 12 of the Local Government Act 2003, the investment would be considered a treasury investment. The advantages of this were that the Council could invest for any purpose. It also preserved a balance of cash above £10 million which allowed the Council to elect to be a Professional client for Markets in Financial Instruments Directive (MiFID II). Under MiFID II, the European Markets in Financial Instrument Directive 2014/65 ("MiFID II") from 3 January 2018, local authorities would lose the automatic right to be categorised as professional clients. However, Members noted that it was expected that Rother would continue to qualify as a professional client.
- The disadvantages were that these investments could be subject to International Financial Reporting Standard (IFRS) 9 which comes in in 2018/19. Under IFRS 9 when investments were rising in value then reserves would increase but a fall in value would reduce the value of reserves. Members needed to be confident that the Council had sufficient levels of reserves to manage these changes.
- There was an increase in risk associated with property related investments and funds would move away from near risk-free cash deposit investments. Property was less liquid and clearly the capital value could fall as well as rise.
- Before any investments were made, Officers would continue discussions with the Council's advisors and the external auditors

taking account of the proposed use of investment powers and any changes finally agreed to treasury and accounting requirements.

The Council would have to borrow to invest beyond the initial £7m; as such it would not be possible to rely on the Section 12 investment powers but rather spending powers. The Government were proposing to require repayments of borrowing (Minimum Revenue Provision, MRP) based on the life of the property asset with a maximum of 40 years for property and 50 years for land. If implemented retrospectively the changes could have significant financial implications for local authorities who have borrowed to fund this type of investment. It was likely that Councils would not have provided for the repayment of the borrowing with the expectation that long term capital property values would exceed the amount of borrowing. With this change the Councils would likely be making a negative return or at best a very small financial margin on the rental returns against the interest costs.

If implemented prospectively then for future investments the financial returns would also be minimal. With such marginality the impact of voids and capital maintenance increased the financial risk and made these investments much less attractive. It may be possible to avoid MRP by how the investment was planned to be managed but this was unclear at present.

The report also provided an update on a number of areas as follows:

- The Council's treasury advisors, Capita Asset Services had provided their view on the current economic climate and their outlook for the remainder of 2017/18, which was appended to the report.
- The Council traditionally made its own investments through the use of call and deposit accounts with the major financial UK institutions; the Council also held a Government Gilt valued at £1.121m which was a legacy of the previous arrangements with external fund managers. The Council had also invested £2.25m in the Churches, Charities, Local Authorities' (CCLA) Property Investment Fund in 2016/17, with a further £2.75m invested at the end of April 2017. The current dividend yield as at September 2017 was 4.60%.
- The Council held £30m of investments at 30 September 2017 and the investment portfolio yield to 30 June 2017 was £85,166K. The Council's budgeted investment return for 2017/18 was £235,000 and the estimated outturn position was £300,000, a surplus of £65,000 which was mainly due to the additional investment in CCLA.

The Council's current treasury management and investment strategies remained robust in managing the Council's cash funds. The economic outlook remained difficult and supported the Council's financial strategy to reduce reliance in investment returns. The Financial Services Manager offered and Members accepted the offer of further training on Treasury Management in light of the proposed changes to the strategy.

RECOMMENDED: That

- 1) the revisions to the Annual Investment Strategy for 2017/18 be approved, as amended as detailed at Appendix A.

RESOLVED: That

- 2) the changes to the Treasury Management Strategy Statement for 2017/18 as set out in Appendix 3 to the report be noted;
- 3) the Chief Finance Officer's (Service Manager - Finance and Welfare) comments on the level of risk set out in paragraphs 11-15 of the report be noted; and
- 4) the Financial Services Manager to provide further training on treasury management as a result of the proposed changes to the strategy.

(Appendix 5 to this matter was considered exempt from publication by virtue of paragraph 5 of Part 1 of Schedule 12A of the Local Government Act 1972, as amended).

PART II DECISIONS TAKEN UNDER DELEGATED POWERS

AS17/33. ANNUAL AUDIT LETTER 2016-17
(6.1)

The Chairman welcomed Leigh Lloyd-Thomas from BDO to the meeting who proceeded to summarise the External Auditors' Annual Audit Letter for the year ended 31 March 2017. The External Auditors' Annual Audit Letter 2016/17 summarised the key issues arising from the work that had been carried out by BDO during the year in the areas of Financial Statements and Use of Resources.

Financial Statements - BDO issued an unmodified true and fair opinion on the financial statements on 27 September 2017. The financial statements prepared for audit was of a very high standard and BDO's audit found no misstatements above the reporting threshold of £20,000.

Use of Resources - BDO issued an unmodified conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources on 27 September 2017.

Whilst there was a significant saving requirement in the Medium Term Financial Strategy to 2020/21, BDO were satisfied that the Council had appropriate arrangements to deliver the planned savings and income growth targets to remain financially sustainable and there was no cause for concern.

It was noted that BDO had reduced the planned fees by £10,000 for the Housing benefits subsidy claim as the Council had employed independent consultants (Branch and Lee) to undertake sample testing of benefits paid in year and BDO were able to use this work to support

the certification review. The final fees for the assurance service was £58,128.

In summary, BDO assured Members that the finances of the Council were being well managed by a well-run team. Members expressed their gratitude to the finance team for keeping the Council's finances in such good order and always being available to answer Members' questions and queries and requested that these sentiments be formally recorded.

RESOLVED: That the report be noted and Members' gratitude to the finance team be formally recorded.

AS17/34.
(6.2)

HOUSING BENEFITS SUBSIDY CERTIFICATION

BDOs' report summarised the main issues arising from the certification of the housing benefits subsidy for the financial year ended 31 March 2017. Local authorities responsible for managing housing benefit were able to claim subsidies towards the cost of these benefits from central Government. BDO had been able to give a good clean opinion for the second year running, which was rare and for which, the Council should be satisfied; Members paid tribute to the benefits team for this remarkable record.

The Public Sector Audit Appointments Ltd (PSAA) had originally set the fees at £20,453, which BDO were able to reduce as reported above at Minute AS17/32. BDO had been able to place reliance on this work and reduce the extent of the testing to be completed. It was noted that Branch and Lee had been paid the sum of £15k for the year to support this and other work but had managed to save the Council at least £130k as part of this work.

BDOs' work on this claim included verifying that the Council was using the correct version of its benefits software and that this software had been updated with the correct parameters. The entries in the claim to underlying records and test a sample of cases from each benefit type confirmed that benefit had been awarded in accordance with the relevant legislation. The methodology and sample sizes were prescribed by the PSAA and the Department for Work and Pensions. The draft subsidy return provided for audit recorded amounts claimed as subsidy of £26,783,474.

RESOLVED: That the report be noted.

AS17/35.
(7.1)

INTERNAL AUDIT REPORT TO 30 SEPTEMBER 2017

The Audit Manager led Members through the internal audit report to 30 September 2017 that gave details of audit matters and any emerging issues not only in relation to audit but risk management and corporate governance. It was advised that good progress continued to be made on the work planned for 2017/18 and the Annual Governance Audits were now well underway.

The report gave details of the four audits completed in the quarter (Planning Income, Car Park Income, Staff Appointments and Data Protection) all of which had given good or substantial assurance on the overall governance arrangements. It was noted that the issues identified with regard to planning income were minor and was largely due to working on two different systems. With regard to car park income, it was confirmed that cash was now collected and credited in a timely manner and a suggestion to provide printed permits, to avoid potential fraud, would be fed back to the team. With regard to data protection, it was advised that the Council was working in partnership with Wealden District Council to ensure that all the necessary arrangements would be in place to comply with the new legislation coming into force in May 2018. There were issues over the personal data held by Councillors on their council and private devices and the level of security required to access such data and these would be addressed in the coming months. It was noted that email accounts of former councillors were closed and no access could be gained to emails etc. once the account was closed.

Work on four other audits (Leisure Centre Contracts, Emergency Planning, Joint Waste Contract – Central Admin and Homelessness Prevention Grants and Loans) was well underway but had been delayed due to work on a special investigation within the housing service.

A recent planned audit of the procedures for awarding grants and loans to housing needs clients had identified a significant financial fraud, perpetrated by a member of the Housing Needs Team over a 16 month period (March 2016 to July 2017), defrauding the Council of £12,550. Members were reassured that as soon as the fraud was discovered, the employee had been dismissed and the case was currently with the Police. Identification of this fraud by Internal Audit was testament to the diligence of their work, and its discovery almost certainly prevented further loss. A number of recommendations had been made to improve internal control as a result of the audit work/internal investigation and further information on the audit findings would be reported to the Audit and Standards Committee in March 2018.

Good progress continued to be made implementing audit recommendations in both the current and previous years. It was noted however that quite a few of the older recommendations (11 Medium and four Low) were yet to be fully implemented and whilst in some cases the reasons were known, in others the reasons were unknown and the Audit Manager would therefore keep the situation under review and escalate any cases to the Executive Directors, as appropriate. There were no high risk recommendations outstanding now that the recommendation in respect of the Asset Management audit had been downgraded to medium risk.

With regard to progress of implementing the single source electronic asset management system, it was advised that as at the end of October 2017, 294 out of 364 records (80%) had been completed. Currently the completion of records was averaging at 26 per month and

the work was estimated to be completed by the end of January 2018, subject to internal validations and checks by audit. It was noted that once all the records had been entered there was sufficient resources to ensure that records would be maintained and kept up to date. In view of progress made, the Audit Manager had downgraded the risk from high to medium. A further progress update would be obtained next quarter to confirm 100% completion; Internal Audit also planned to carry out a review of Asset Management in 2018/19 and this would identify any residual issues.

RESOLVED: That the Internal Audit report to 30 September 2017 be noted.

AS17/36.
(7.3)

ANNUAL RISK MANAGEMENT UPDATE

Members considered the annual update report that covered progress in Risk Management during 2017. Risk referred to the uncertainty that surrounded future events and outcomes and it was essential that the Council had a strong approach to Risk Management, particularly with the current environment of substantial financial and resource pressures.

The issue of Risk Management was reviewed every six months by the Strategic Management Team and Service Managers; recent exercises included issues of pension fund failure and a heightened warning of terrorist incidents and associated plans had been updated. It was noted that Risk Management training was now a regular feature of the Sussex Training Consortium programme.

The Corporate Risk Framework attached at Appendix A to the report had been updated during the year and the following key changes had been made:

- The addition of a heightened warning of a terrorist incident as a Corporate Risk (primarily around Town Hall operations).
- Adjustment of some of the risk ratings in the light of new information.

The Committee noted that the Corporate Risk Framework was a live document and the likelihood, impact and ratings could change frequently depending on many factors, including the Council's financial situation. As a consequence of the Grenfell disaster, it was noted that neither the Council or its Registered Social Landlords owned any high rise clad properties in Rother, however, the Council had a duty to have emergency planning measures in place to support communities in times of crisis, both in private and public sector ownerships and the impact this would have on the Council was on the risk register (18).

RESOLVED: That the report be noted.

AS17/37.
(7.4) **WORK PROGRAMME**

Consideration was given to the Work Programme which contained details of the reports to be considered by the Audit and Standards Committee meetings until July 2018. It was noted that an additional meeting was required to enable preparation of the Statement of Accounts and this was proposed for Wednesday 25 July, at a time to be agreed by the Committee. It was agreed that the meeting would take place at the usual start time of 6.30pm.

RESOLVED: That the

- 1) additional meeting date of Wednesday 25 July at 6.30pm be noted; and
- 2) Work Programme at Appendix B be approved.

AS17/38.
(8.1) **PROPERTY INVESTMENT PANEL**

In October 2017, Cabinet referred a recommendation to Council that an initial budget of £7m for acquisitions of investment properties be approved. If approved by Council at its meeting on 18 December, a Property Investment Panel (PIP) would be required to make recommendations to the Head of Paid Service of those properties to be acquired.

Whilst the Council set the overall investment strategy, the Audit and Standards Committee would be responsible for monitoring throughout the year the performance of any investments made using the Council's treasury management powers. It was therefore necessary for the Audit and Standards Committee to consider the governance and risk management arrangements detailed in the report. Members were satisfied with the governance and risk arrangements of the proposed PIP.

RESOLVED: That the report be noted.

CHAIRMAN

The meeting closed at 7:56pm

as171211/ljc

Treasury Management Practice – Credit and Counterparty Risk

Specified Investments:

1. All such investments will be sterling denominated, with maturities up to maximum of 1 year, meeting the minimum 'high' quality criteria where applicable.
2. A variety of investment instruments will be used, subject to the credit quality of the institution, and depending on the type of investment made it will fall into one of the following categories:

| | Minimum Credit Criteria | Maximum of total investments | Max. maturity period |
|--|----------------------------------|------------------------------|------------------------------|
| Debt Management Agency Deposit Facility | -- | 100% | 6 months |
| Local authorities | -- | 50% | 1 year subject to guidance |
| UK banks and building societies | Refer to Creditworthiness Policy | 100% | 1 year |
| Term deposit - UK banks and building societies | Refer to Creditworthiness Policy | 100% | 1 year |
| UK Government Gilts | UK sovereign rating | 50% | 1 year subject to guidance |
| Bonds issued by multilateral development banks | AAA | 20% | 6 months subject to guidance |
| Ultra-Short Dated Bond Funds with a credit score of 1.25 | AAA | 100% | Liquid |
| Ultra-Short Dated Bond Funds with a credit score of 1.5 | AAA | 100% | Liquid |
| Money Market Funds | AAA | 100% | Liquid |
| CDs or corporate bonds with banks and building societies | Refer to Creditworthiness Policy | 20% | 1 year |
| UK Government Treasury Bills | UK sovereign rating | 20% | 1 year |

Accounting treatment of investments. The accounting treatment may differ from the underlying cash transactions arising from investment decisions made by this Council. To ensure that the Council is protected from any adverse revenue impact,

which may arise from these differences, we will review the accounting implications of new transactions before they are undertaken.

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 sterling investments.

Non-specified investments A maximum of £15 million will be held in aggregate in non-specified investment.

Maturity greater than 1 year.

| | Non Specified Investment Category | Limit (£ or %) |
|----|--|---|
| a. | <p>Supranational bonds greater than 1 year to maturity</p> <p>(a) Multilateral development bank bonds – these are bonds defined as an international financial institution having as one of its objects economic development, either generally or in any region of the world (e.g. European Reconstruction and Development Bank etc.).</p> <p>(b) A financial institution that is guaranteed by the United Kingdom Government (e.g. National Rail, the Guaranteed Export Finance Company [GEFCO])</p> <p>The security of interest and principal on maturity is on a par with the Government and so very secure. These bonds usually provide returns above equivalent gilt edged securities. However the value of the bond may rise or fall before maturity and losses may accrue if the bond is sold before maturity.</p> | AAA long term ratings (or other of your choice) |
| b. | The Council's own banker if it fails to meet the basic credit criteria. In this instance balances will be minimised as far as is possible. | |
| c. | Certificates of deposit issued by banks and building societies. Refer to Creditworthiness Policy | £3m – 10% of fund |
| d. | Property funds – the use of these instruments can be deemed to be capital expenditure, and as such will be an application (spending) of capital resources. This Authority will seek guidance on the status of any fund it may consider using. | Officers in consultation with the Council's treasury advisers |
| e. | Property purchases. The criteria for any purchase of property for investment purposes will meet the following broad criteria in the approved Property Investment Strategy (PIS) – Appendix 4. Appropriate due diligence will also be undertaken before investment of this type is undertaken. | In accordance with the PIS governance arrangements |

AUDIT AND STANDARDS COMMITTEE

| WORK PROGRAMME 2017 – 2018 | |
|-----------------------------------|---|
| DATE OF COMMITTEE | SUBJECT |
| Monday 26 March 2018 | <p>Part A – Standards Reports (none scheduled)</p> <p>Part B – Audit Reports</p> <ul style="list-style-type: none"> • BDO – Audit Plan 2017-18 • Internal Audit Report to 31 December 2017 • Annual Governance Statement 2017/18 • Internal Audit Plan 2018-19 • Review of Internal Audit 2017-18 • Treasury Management Report • Report on the respective roles of Members and Officers in the development of policies and the operational implementation of those policies. |
| Monday 25 June 2018 | <p>Part A – Standards Reports</p> <ul style="list-style-type: none"> • Code of Conduct Complaints Monitoring. • Ombudsman Complaints Monitoring. <p>Part B – Audit Reports</p> <ul style="list-style-type: none"> • Internal Audit Report to 31 March 2017 • Treasury Management Report – 2017/18 Outturn |
| Wednesday 25 July 2018 | <p>Part A – Standards Reports (none scheduled)</p> <p>Part B – Audit Reports</p> <ul style="list-style-type: none"> • BDO – Annual Governance Report 2017/18 • Statement of Accounts 2017/18 |