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Chairman and Members of the
Audit and Governance Committee

Your contact: Peter Mannings
Tel: 01279 502174
Date: 29 January 2024

cc. All other recipients of the Audit
and Governance Committee agenda

Dear Councillor,

AUDIT AND GOVERNANCE COMMITTEE - 30 JANUARY 2024

Please find attached the following reports which were marked “to follow” on the agenda for the above meeting:

5. External Audit Planning Report 2023/24 (Pages 3 - 33)
7. Treasury Management Review Mid-Year Review 2023/24 (Pages 34 - 48)
8. Capital Strategy and Minimum Revenue Provision Policy, Treasury Management Strategy 2024/25 (Pages 49 - 89)
9. Financial Management 2023/24 – Quarter 2 Forecast to Year End (Pages 90 - 105)
14. Audit and Governance Committee Work Programme (Pages 106 - 121)

Please read these papers before the meeting tomorrow evening.

Yours faithfully,

Peter Mannings
Democratic Services Officer
East Herts Council
peter.mannings@eastherts.gov.uk

MEETING : AUDIT AND GOVERNANCE COMMITTEE
VENUE : COUNCIL CHAMBER, WALLFIELDS, HERTFORD
DATE : TUESDAY 30 JANUARY 2024
TIME : 7.00 PM

East Herts Council Report

Audit and Governance Committee

Date of meeting: 30 January 2024

Report by: Steven Linnett, Head of Strategic Finance and Property (Section 151 Officer)

Report title: Receipt of the External Auditor's Audit Planning Report 2023/24

Ward(s) affected: All

Summary

- The external auditor will present their Audit Planning Report 2023/24 to the Committee setting out the planning for the audit of the 2023/24 statement of accounts.

RECOMMENDATIONS FOR AUDIT AND GOVERNANCE COMMITTEE:

(A) Receive and make any comments on the external auditor's Provisional Audit Planning Report 2023/24.

1.0 Proposal(s)

1.1 The 2023/24 audit of the statement of accounts will be undertaken by Azets who were appointed by Public Sector Audit Appointments Limited. The plan sets out the auditor's planned work to deliver an opinion on the 2023/24 statement of accounts, their assessment of risk and indicative fee levels.

1.2 The report and proposals are the external auditor's and whilst officers are consulted on factual accuracy, they have no ability

to change anything in the report.

- 1.3 The external auditor's Provisional Audit Planning Report for 2023/24 is attached at **Appendix A**.
- 1.4 The scale fee is set by Public Sector Audit Appointments Limited (PSAA) and for the 2023/24 audit will be £236,822 which includes a one-off fee of £18,500 to verify the data transfer from the current on premise financial management system to a cloud based solution. Excluding this one off item the audit fee will increase by 98.8% which is in line with the guide issued by PSAA that councils should expect fees to increase by at least 100%.

2.0 Background

- 2.1 The local public audit market has effectively been dysfunctional since 2020 and there have been severe delays to local authority audits. The council's 2020/21 accounts only received an audit opinion on 16 March 2023. The 2021/22 accounts audit is still in progress and EY have stated that if they can they intend to undertake no work on the 2022/23 accounts. The delay to the audit is due to the external auditor not having sufficient resources to undertake the audit. The [Redmond Review](#) of the local audit market provides useful background information for Members.
- 2.2 The 2023/24 to 2027/28 audits were subject to a competitive tendering exercise undertaken by Public Sector Audit Appointments Limited and Azets Audit Services has been appointed for this period.
- 2.3 The Government has announced they intend to intervene to try and bring the backlog to an end and may allow auditors to disclaim an opinion or to leave a financial year unaudited. This has huge implications for the 2023/24 financial year as

Azets will be unable to issue a clean audit opinion as the brought forward balances would be unaudited. The Government promised further updates in September 2023 and none has been forthcoming to date. The Committee will be updated when Government issue further updates.

3.0 Reason(s)

3.1 The external auditor is required by auditing standards to present the Committee with their Audit Planning Report.

4.0 Options

4.1 Members can ask questions and make observations to the external auditor but they cannot reject the Provisional Audit Planning Report.

5.0 Risks

5.1 The delay to the completion of the audits means that it may affect the council's audit for 2023/24 and mean a clean audit opinion cannot be issued.

5.2 The production of the budget alongside the audit in the last two years has placed a huge strain on resources and required the Head of Strategic Finance & Property and senior officers in Finance to work long hours and led to the process being both stressful and less than efficient than in previous years. Senior officers had to roll up their sleeves and undertake a lot of work usually undertaken by junior staff. This situation has occurred for the last two years and it looks likely to continue for the next two.

5.3 A number of staff are due to reach retirement age in the next 24 months so there is a risk that it will not be possible to recruit suitable replacement staff, particularly qualified staff,

due to the national shortage of local authority accountants.

6.0 Implications/Consultations

Community Safety

No

Data Protection

No

Equalities

No

Environmental Sustainability

No

Financial

These are contained in the main body of the report

Health and Safety

No

Human Resources

These are contained in the main body of the report

Human Rights

No

Legal

No

Specific Wards

No

7.0 Background papers, appendices and other relevant material

Appendices:

Appendix A –Audit Planning Report 2023/24

Background Papers:

None

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Report Author

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East Hertfordshire District Council

External audit plan

Year ended 31 March 2024

November 2023



Your key team members

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Adding value through the audit

All our clients demand of us a positive contribution to meeting their ever-changing business needs. Our aim is to add value to the Council through our external audit work by being constructive and forward looking, by identifying areas of improvement and by recommending and encouraging good practice. In this way, we aim to help the Council promote improved standards of governance, better management and decision making and more effective use of resources.

Purpose

This audit plan highlights the key elements of our proposed audit strategy and provides an overview of the planned scope and timing of the statutory external audit of East Hertfordshire District Council ('the Council') for the year ended 31 March 2024 for those charged with governance.

The core elements of our work include:

- An audit of the 2023/24 Statement of Accounts for the Council and its Group; and
- An assessment of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources (our Value for Money work).

We will conduct our audit in accordance with International Standards on Auditing (ISAs) (UK), the Local Audit and Accountability Act 2014 (the 'Act'), and the National Audit Office Code of Audit Practice. The Code of Audit Practice sets out what local auditors of relevant local public bodies are required to do to fulfil their statutory responsibilities under the Act.

Auditor responsibilities

As auditor we are responsible for performing an audit, in accordance with the Local Audit and Accountability Act 2014, the Code of Audit Practice issued by the National Audit Office and ISAs UK. Our primary responsibility is to form and express an independent opinion on the Council's and its Group's financial statements, stating whether they provide a true and fair view and have been prepared properly in accordance with applicable law and the CIPFA Code of Practice on Local Authority Accounting in the UK (the 'CIPFA Code').

We are also required to:

- Report on whether the other information included in the Statement of Accounts (including the Narrative Report and Annual Governance Statement) is consistent with the financial statements;
- Report by exception if the disclosures in the Annual Governance Statement are incomplete or if the Annual Governance Statement is misleading or inconsistent with our knowledge acquired during the audit;
- Report by exception any significant weaknesses identified in arrangements for securing value for money and a summary of associated recommendations;
- Report by exception on the use of our other statutory powers and duties; and
- Certify completion of our audit.

Introduction

We will conduct our audit in accordance with International Standards on Auditing (ISAs) (UK), the Local Audit and Accountability Act 2014 (the 'Act'), and the National Audit Office Code of Audit Practice. The Code of Audit Practice sets out what local auditors of relevant local public bodies are required to do to fulfil their statutory responsibilities under the Act.

This planning letter has been prepared for the sole use of those charged with governance and management and should not be relied upon by third parties. No responsibility is assumed by Azets Audit Services to third parties.

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Auditor responsibilities (*....continued*)

We will issue our Audit Findings Report and an Auditors Annual Report to the Audit Committee setting out the findings from our work. Under the Act we have a broad range of reporting responsibilities and powers that are unique to the audit of local authorities in the United Kingdom. These include:

- Reporting matters in the public interest;
- Making written recommendations to the Council;
- Making an application to the court for a declaration that an item of account is contrary to law;
- Issuing and advisory notice; or
- Making an application for judicial review.

The Act also requires us to give an elector, or any representative of the elector, the opportunity to question us about the accounting records of the Council and consider any objection made to the accounts.

On completion of our audit work, we will issue an Audit Findings Report (prior to the approval of the financial statements), detailing our significant findings and other matters arising from the audit on the financial statements, together with an Auditor's Annual Report including our commentary on the value for money arrangements.

If, during the course of the audit, we identify any significant adverse or unexpected findings that we conclude should be communicated, we will do so on a timely basis, either informally or in writing.

The audit does not relieve management or the Audit Committee of your responsibilities, including those in relation to the preparation of the financial statements.

Council responsibilities

The Council has responsibility for:

- Preparing financial statements which give a true and fair view, in accordance with the applicable financial reporting framework and relevant legislation;
- Preparing and publishing, along with the financial statements, an annual governance statement and narrative report;
- Maintaining proper accounting records and preparing working papers to an acceptable professional standard that support its financial statements and related reports disclosures; and
- Ensuring the proper financial stewardship of public funds, complying with relevant legislation and establishing effective arrangements for governance, propriety and regularity.

Audit scope and general approach

This section of our letter sets out the scope and nature of our audit and should be considered in conjunction with the [Terms of Appointment](#) and [Statement of Responsibilities](#) issued by Public Sector Audit Appointments Limited (PSAA).

General approach

Our objective when performing an audit is to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement and to issue an auditor's report that includes our auditor's opinion.

As part of our risk-based audit approach, we will:

- Perform risk assessment procedures including updating our understanding of the Council and its Group, including its environment, the financial reporting framework and its system of internal control;
- Review the design and implementation of key internal controls;
- Identify and assess the risks of material misstatement, whether due to fraud or error, at the financial statement level and the assertion level for classes of transaction, account balances and disclosures;

- Design and perform audit procedures responsive to those risks, to obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion; and
- Exercise professional judgment and maintain professional scepticism throughout the audit recognising that circumstances may exist that cause the financial statements to be materially misstated.

We will undertake a variety of audit procedures designed to provide us with sufficient evidence to give us reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

We include an explanation in the auditor's report of the extent to which the audit was capable of detecting irregularities, including fraud and respective responsibilities for prevention and detection of fraud.

Audit scope and general approach

Materiality

We apply the concept of materiality both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements.

Judgments about materiality are made in the light of surrounding circumstances and are affected by our perception of the financial information needs of users of the financial statements, and by the size or nature of a misstatement, or a combination of both. **The basis for our assessment of materiality for the year is set out in Appendix I.**

Any identified errors greater than:

£72,500

Will be recorded and discussed with you and, if not adjusted, confirmed as immaterial as part of your letter of representation to us.

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Accounting systems and internal controls

The purpose of an audit is to express an opinion on the financial statements. We will follow a substantive testing approach to gain audit assurance rather than relying on tests of controls. As part of our work, we consider certain internal controls relevant to the preparation of the financial statements such that we are able to design appropriate audit procedures. However, this work does not cover all internal controls and is not designed for the purpose of expressing an opinion on the effectiveness of internal controls. If, as part of our consideration of internal controls, we identify significant deficiencies in controls, we will report these to you in writing.

Specialised skill or knowledge required to complete the audit procedures

We will use audit specialists to assist us in our audit work in the following areas:

- The audit of the actuarial assumptions used in the calculation of the defined benefit pension liability/asset; and
- The audit of investment or property valuations, should the need arise during the course of the audit.

We will consult internally with our Technology Risk team for them to support the audit team by assessing the information technology general controls (ITGC) of your systems, including your general financial ledger.

Audit scope and general approach

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Significant changes in the financial reporting framework

There have been no significant changes in the financial reporting framework this year, including the CIPFA Code of Practice on Local Authority Accounting in the United Kingdom (the 'CIPFA Code'). As permitted by the CIPFA Code the council has chosen to defer the implementation of IFRS 16 'Leases' until 2024/25.

Significant changes in the Council's (and Group's) functions or activities

There have been no significant changes to the functions and activities of the Council or its group structure. We have not been made aware of any significant changes in the functions or activities of the other components in the Council's group.

Our group audit scope and risk assessment is set out in Appendix II.

Going concern

Management responsibility

Management is required to make and document an assessment of whether the Council [and group] is a going concern when preparing the financial statements. The review period should cover at least 12 months from the date of approval of the financial statements. Management are also required to make balanced, proportionate and clear disclosures about going concern within the financial statements where material uncertainties exist in order to give a true and fair view.

Going concern

Auditor responsibility

Under ISA (UK) 570, we are required to consider the appropriateness of management's use of the going concern assumption in the preparation of the financial statements and consider whether there are material uncertainties about the Council [and group]'s ability to continue as a going concern that need to be disclosed in the financial statements.

In assessing going concern, we will consider the guidance published in the CIPFA Code and Practice Note 10 (PN10), which focusses on the anticipated future provision of services in the public sector rather than the future existence of the entity itself.

Audit scope and general approach

Related party transactions

ISA 550 requires that the audit process starts with the audited body providing a list of related parties to the auditor, including any entities under common control. During our initial audit planning you have informed us of the individuals and entities that you consider to be related parties. Please advise us of any changes as and when they arise.

Additional procedures for the NAO

The National Audit Office (the 'NAO') issues group audit instructions which set out additional audit requirements. We expect the procedures for this year to be similar to previous years.

The NAO audit team for the WGA request us to undertake specific audit procedures in order to provide them with additional assurance over the amounts recorded in WGA schedules. The extent of these procedures will depend on whether the Council has been selected by the NAO as a sampled component for 2023/24. As at the date of this report, the draft instructions have not yet been issued by the NAO and the NAO have not yet confirmed which entities will be sampled components.

We will seek to comply with the instructions and to report to the NAO in accordance with their requirements once instructions have been issued.

Auditor reporting delays for previous periods and the impact on our audit

Although we are planning to complete your audit for the year ended 31 March 2024 in line with the timetable set out on page 17, so that we can report our initial findings to your Audit Committee in November 2024, please note that we will not be able to fully complete our audit, issue our auditor's report and certify the closure of the audit until your predecessor auditor has completed their audit for the year ended 31 March 2023. Once the 2023 audit has been completed we will need to review the predecessor auditor's audit file to gain assurance over your opening balances as at 1 April 2023, and consider the impact on our audit of any modifications to their auditor's report.

Further, once the 2023 audit, and earlier years has been completed, we will revisit our planning procedures and audit plan to assess whether any additional procedures are required over and above those we have identified in this audit plan. Should additional procedures or changes to the plan be required, we will report these to you. The cost of additional work to revisit planning upon completion of the prior year audits will also be reported to you.

Audit scope and general approach

Continued progress of the audit

We have held meetings with the Director of Finance and Chief Executive to inform our planning.

Management has not been able to respond to detailed information requests so far, due to their need to spend time dealing with their predecessor auditors in respect of the open audits for earlier years. In particular, we are awaiting responses to the following essential requests to finalise our planning:

- Responses to management enquiries regarding planned use of estimates, group structure, going concern and laws and regulations, amongst others
- Responses from those charged with governance in respect of their oversight of management's work
- Detailed review of internal audit work and relevant contact details

- Detailed budgetary plans and financial performance monitoring for the year to date
- Management self-assessment of arrangements in place to support the achievement of value for money
- Provision of information in response to planning enquiries

The above list is not exhaustive.

The continued progression of the audit from this point is dependant upon management's capacity to respond to requests and provide information as required. In particular, our planned timeframe for the interim audit in early 2024 and final accounts audit in Autumn 2024 can only be met once management is able to satisfy the required information requests. Should this not be possible, we will inform you of the change to the audit timescales and revised likely completion dates.

Should anything arise from our finalisation of the planning procedures that changes the risks or planned procedures set out in this document, we will report these to you.

Significant risks of material misstatement

Significant risks are risks that require special audit consideration and include identified risks of material misstatement that:

- Our risk assessment procedures have identified as being close to the upper range of the spectrum of inherent risk due to their nature and a combination of the likelihood and potential magnitude of misstatement; or
- Are required to be treated as significant risks due to requirements of ISAs (UK), for example in relation to management override of internal controls.

Significant risks at the financial statement level

The table below and overleaf summarises significant risks of material misstatement identified at the financial statement level. These risks are considered to have a pervasive impact on the financial statements as a whole and potentially affect many assertions for classes of transaction, account balances and disclosures.

Identified risk	Planned audit procedures
<p>Management override of controls</p> <p>Auditing Standards require auditors to treat management override of controls as a significant risk on all audits. This is because management is in a unique position to perpetrate fraud by manipulating accounting records and overriding controls that otherwise appear to be operating effectively.</p> <p>Although the level of risk of management override of controls will vary from entity to entity, the risk is nevertheless present in all entities.</p> <p>Specific areas of potential risk including manual journals, management estimates and judgements and one-off transactions outside the ordinary course of the business.</p> <p>Risk of material misstatement: Very High</p>	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Documenting our understanding of the journals posting process and evaluating the design effectiveness of management controls over journals; • Analysing the journals listing and determining the criteria for selecting high risk and/or unusual journals; • Testing high risk and/or unusual journals posted during the year and after the draft accounts stage back to supporting documentation for appropriateness, corroboration and to ensure approval has been undertaken in line with the Council's journals policy; • Gaining an understanding of the key accounting estimates and critical judgements made by management. We will also challenge assumptions and consider for reasonableness any indicators of bias which could result in material misstatement due to fraud; and • Evaluating the rationale for any changes in accounting policies, estimate or significant unusual transactions.

Significant risks of material misstatement

Identified risk	Planned audit procedures
<p>Prior year opinion on the financial statements</p> <p>As at the date of writing, you have not been able to obtain an unmodified opinion from your predecessor auditor for the 2022/23 financial year. In addition, the opinions for the financial years 2021/22 and 2020/21 have not yet been issued.</p> <p>There is therefore a risk that issues not yet identified in the open audit years arise in the completion of those audits which may impact the current (2023/24) audit year.</p> <p>There is a further risk that, in the event an ‘audit backstop’ is implemented for 31 March 2024, the prior year period opinions may be qualified by a ‘limitation of scope’ or disclaimed in full.</p> <p>In this eventuality:</p> <ul style="list-style-type: none"> • there may be limited assurance available over the Council’s opening balances, including those balances which involve higher levels of management judgement and more complex estimation techniques (e.g. defined benefit pensions valuations and property, plant and equipment valuations, amongst others). • significant transactions, accounting treatment and management judgements may not have been subject to audit for one or more years – or at all. This may include management judgements and accounting treatment in respect of significant new schemes (such as major capital initiatives), changes to group structures or other significant accounting treatments which came into effect during the qualified or disclaimed period, going back to 2019/20. <p>The potential absence of prior year assurance raises a significant risk of material misstatement at the financial statements level that may require additional audit procedures.</p> <p>Risk of material misstatement: High</p>	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Considering the findings and outcomes of unfinished prior year audits and their impact on the 2023/24 audit; • Considering the impact on our work of the impact of qualified or disclaimed audit opinions, particularly regarding opening balances and ‘unaudited’ transactions and management judgements made in the previous years which continue into 2023/24; and • Considering the impact of any changes in Code requirements for financial reporting in previous and current audit years

Significant risks of material misstatement

Identified risk	Planned audit procedures
<p>Change in the Financial System</p> <p>You plan to transfer your core financial system to a new, cloud-based system from 1 April 2024. Whilst the transfer will take place from the first day of the next financial year, management have informed us they plan to close the 2023/24 financial year on the new system.</p> <p>There is an inherent risk over the completeness and accuracy of data transfer from the old system to the new system. As the financial statements for 2023/24 will be produced using the transferred data from the new system, the transfer therefore presents a risk that errors in the transfer could lead to material misstatements in the accounts.</p> <p>Risk of material misstatement: High</p>	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Gaining an understanding of the processes and controls put in place by management to ensure that the transfer of data is complete, accurate, and not materially misstated and evaluate the design of the associated controls • Reviewing and assessing assurance reports provided by the council on the implementation of the new financial system, on which management are relying to satisfy themselves over the completeness and accuracy of the data transfer. • Reviewing and assessing any assurance provided by internal audit assurance from reviews undertaken by them over the transfer. • Undertaking procedures to gain assurance over the completeness of the data transferred • Undertaking testing, on a sample basis, over the accuracy of data transferred, both from the old system to the new, and from the new system back to the source data on the old system. <p>We will use our specialist Risk and Technology Assurance team to assess the IT related control risks inherent in the transfer.</p>

Significant risks of material misstatement

Significant risks at the assertion level for classes of transaction, account balances and disclosures

The table below summarises significant risks of material misstatement at the assertion level for classes of transaction, account balances and disclosures.

Identified risk	Planned audit procedures
<p>Fraud in revenue recognition and expenditure (rebutted)</p> <p>Material misstatement due to fraudulent financial reporting relating to revenue recognition is a rebuttable presumed risk in ISA (UK) 240.</p> <p>Having considered the nature of the revenue streams at the Council, we consider that the risk of fraud in revenue recognition can be rebutted on all income streams because:</p> <ul style="list-style-type: none"> • there is little opportunity available to manipulate revenue recognition; • there is limited incentives to manipulate revenue recognition • the Council's existing income transactions do not provide a significant opportunity to manipulate income between years in any meaningful way or to adopt aggressive recognition policies. <p>We have also considered Practice Note 10, which comments that for certain public bodies, the risk of manipulating expenditure could exceed the risk of the manipulation of revenue. We have therefore also considered the risk of fraud in expenditure at the Council, and we are satisfied that this is not a significant risk for the reasons set out above.</p> <p>Inherent risk of material misstatement:</p> <ul style="list-style-type: none"> • Revenue and expenditure recognition: Low 	<p>Whilst we have rebutted the risk of fraud in income and expenditure, we will perform the below procedures based on their value within the financial statements:</p> <ul style="list-style-type: none"> • Documenting our understanding of the Council's systems for income and expenditure to identify significant classes of transactions, account balances and disclosures with a risk of material misstatement in the financial statements • Evaluating the Council's accounting policies for recognition of income and expenditure and compliance with the CIPFA Code. • Substantively testing material income and expenditure streams using analytical procedures and sample testing of transactions recognised for the year.

Significant risks of material misstatement

Identified risk	Planned audit procedures
<p>Valuation of other land and buildings and investment property (key accounting estimate) Council and group</p> <p>The Council carries out revaluations of both their property, plant and equipment and its investment property annually.</p> <p>Management engage the services of their in-house Estate and Asset Managers, Anna Osborne and Lucy Smith who are Regulated Members of the Royal Institute of Chartered Surveyors (RICS) to undertake these valuations as at 31 March 2024.</p> <p>The valuations involve a wide range of assumptions and source data and are therefore sensitive to changes in market conditions. ISAs (UK) 500 and 540 require us to undertake audit procedures on the use of external expert valuers and the methods, assumptions and source data underlying the fair value estimates.</p> <p>This represents a key accounting estimate made by management within the financial statements due to the size of the values involved, the subjectivity of the measurement and the sensitive nature of the estimate to changes in key assumptions. We have therefore identified the valuation of land and buildings and investment property as a significant risk.</p> <p>We will further pinpoint this risk to specific assets, or asset types, on receipt of the draft financial statements and the year-end updated asset valuations to those assets where the in-year valuation movements falls outside of our expectations.</p> <p>Inherent risk of material misstatement:</p> <ul style="list-style-type: none"> • Land and buildings and investment property (valuation): Very High 	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Consulting with management to update our understanding on the approach taken by the management in its valuation of Council land and buildings and investment properties, including review and challenge of the methodology that the client uses. • Reviewing the scope and terms of work with the asset management team • Assessing how management use the asset management team report to value land and buildings and investment properties in the financial statements • Reviewing the valuation approach and assessment in respect of capital additions within the year to ensure we understand how valuations have been updated and amended as the assets have been brought into use • Consideration of engagement of Azets valuation specialists to assist the audit team on a sample of assets, based on our assessment of the asset valuations subject to a higher degree of risk for their valuations as at 31 March 2024. • Contacting the asset management team to obtain information on the methodology and their procedures to ensure objectivity and quality, including compliance with professional standards • Where material, we will also test a sample of valuation movements to gain assurance that the accounting treatment is appropriate, and we will also consider evidence of regional valuation trends.

Significant risks of material misstatement

Identified risk	Planned audit procedures
<p>Valuation of the defined pension fund net liability/asset (key accounting estimate) Council and group</p> <p>An actuarial estimate of the net defined pension liability/asset is calculated on an annual basis under IAS 19 'Employee Benefits', and on a triennial funding basis, by an independent firm of actuaries with specialist knowledge and experience. The triennial estimates are based on the most up to date membership data held by the pension fund and a roll forward approach is used in intervening years, as permitted by the CIPFA Code.</p> <p>The calculations involve a number of key assumptions, such as discount rates and inflation and local factors such as mortality rates and expected pay rises. The estimates are highly sensitive to changes in these assumptions and the calculation of any asset ceiling when determining the value of a pension asset. ISAs (UK) 500 and 540 require us to undertake audit procedures on the use of external experts (the actuary) and the methods, assumptions and source data underlying the estimates.</p> <p>This represents a key accounting estimate made by management within the financial statements due to the size of the values involved, the subjectivity of the measurement and the sensitive nature of the estimate to changes in key assumptions. We have therefore identified the valuation of the net pension liability/asset as a significant risk.</p> <p>Inherent risk of material misstatement:</p> <ul style="list-style-type: none"> • Defined pension fund net liability/asset (valuation): High 	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Evaluating managements processes for the calculation of the estimate, the instructions issued to management's expert (the actuary) and the scope of their work; • Evaluating the competence, capabilities and objectivity of the actuary; • Assessing the controls in place to ensure that the data provided to the actuary by the Council and their pension fund was accurate and complete; • Evaluating the methods, assumptions and source data used by the actuary in their valuations, with the support of an auditors' expert; • Evaluating whether any asset ceiling was appropriately considered (if applicable) when determining the value of any pension asset included in the financial statements; • Assessing the impact of any significant differences between the estimated gross asset valuations included in the financial statements and the Council's share of the investment valuations in the audited pension fund accounts' and • Ensuring pension valuation movements for the year and related disclosures have been correctly reflected in the financial statements.

Significant risks of material misstatement

Identified risk	Planned audit procedures
<p>Incorrect capitalisation of revenue expenditure Council and group</p> <p>We have assessed that the risk of misreporting revenue outturn in the financial statements is most likely to be achieved through:</p> <ul style="list-style-type: none"> • Revenue expenditure being inappropriately recognised as capital expenditure at the point it is posted to the general ledger. • Expenditure being inappropriately transferred by journal from revenue to capital codes on the general ledger at the end of the year. <p>If this were to happen it would have the impact of understating revenue expenditure and overstating property, plant and equipment additions in the financial statements.</p> <ul style="list-style-type: none"> • Revenue expenditure: High • Property, plant and equipment additions: High 	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Obtain a general ledger breakdown of capital additions in the year, reconcile this to the Fixed Assets Register and review the general ledger descriptions to identify whether there are any potential transactional items that could be revenue in nature; • Sample test additions to property, plant and equipment to ensure they have been correctly classified as capital and included at the correct value in order to identify any revenue items that have been inappropriately capitalised. We review the sample selected against the definition of capital expenditure in IAS 16 • As part of our journals testing strategy, we will review unusual journals transferring expenditure from revenue to capital codes on the general ledger at the end of the year

Other risks of material misstatement

Other identified risks

Other identified risks are those which, although not considered to be significant, will require specific consideration during the audit.

Identified risk	Planned audit procedures
<p>Minimum revenue provision</p> <p>Linked to the risk of ‘misstatements due to fraud and error’, we consider specific areas where management makes significant judgements that impact charges to the General Fund balance.</p> <p>Local authorities are required to charge a ‘Minimum Revenue Provision’ (MRP) to the General Fund in each financial year related to borrowing. The calculation of this charge is based on the Capital Financing Requirement. Local authorities have flexibility in how they calculate MRP, but need to ensure the calculation is prudent. In calculating a prudent provision, local authorities are required to have regard to statutory guidance.</p> <p>There is a risk that the Council may not been appropriately prudent in its calculation of MRP and/or not followed the relevant statutory guidance.</p>	<p>Procedures performed to mitigate risks of material misstatement in this area will include:</p> <ul style="list-style-type: none"> • Gaining an understanding of the processes and controls put in place by management to calculate Minimum revenue provision • Assessing and reviewing the calculation of the Capital Financing Requirement to ensure it is appropriate and consistent with other notes in the financial statements • Evaluating the appropriateness of the Council’s MRP policy • Evaluating whether MRP has been appropriately calculated in accordance with the revised statutory guidance.

Other material balances and transactions

Under International Standards on Auditing, “irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance and disclosure”. All other material balances and transaction streams will therefore be audited. However, the procedures will not be as extensive as those adopted for the risks identified in this report.

Value for Money arrangements

Under the Code of Audit Practice, we must satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources (referred to here as “Value for Money”, or “VFM”).

NAO Auditor Guidance Note 03 ‘Auditors’ Work on Value for Money Arrangements’ (“AGN 03”) was updated and issued on 18 January 2023 and requires us to provide an annual commentary on arrangements, which will be published as part of the Auditor’s Annual Report. Such commentary will highlight any significant weaknesses in arrangements, along with recommendations for improvements.

When reporting on such arrangements, the Code of Practice requires us to structure our commentary under three specified reporting criteria:

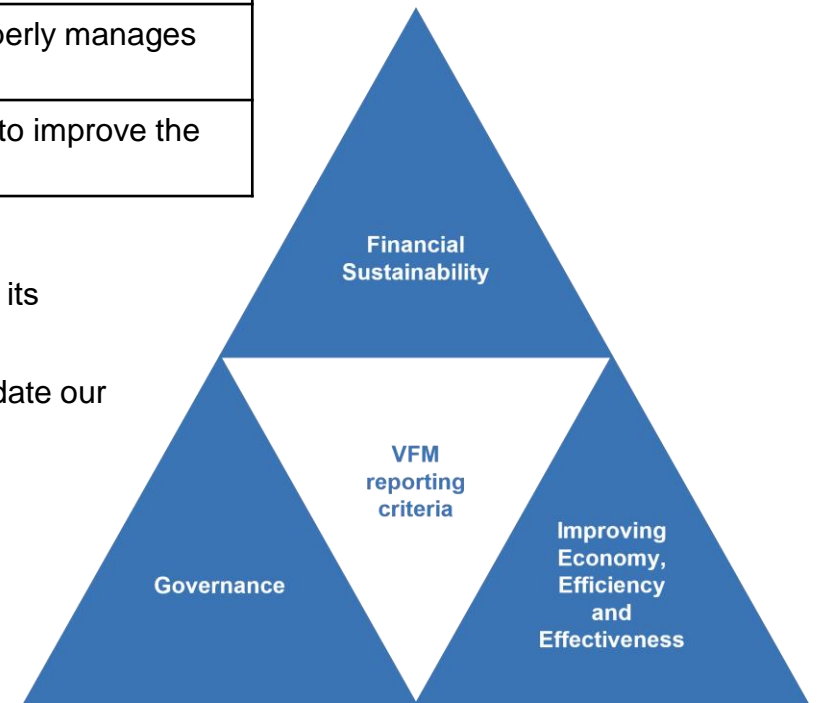
Financial sustainability	How the body plans and manages its resources to ensure it can continue to deliver its services
Governance	How the body ensures that it makes informed decisions and properly manages its risks
Improving economy, efficiency and effectiveness	How the body uses information about its costs and performance to improve the way it manages and delivers its services

As part of the planning process, we are required to perform procedures to identify potential risks of significant weaknesses in the Council’s arrangements to secure VFM through the economic, efficient and effective use of its resources.

We are required to re-evaluate this risk assessment during the course of the audit and, where appropriate, update our work to reflect emerging risks or findings that may suggest a significant weakness in arrangements.

Where we identify significant weaknesses in arrangements as part of our work, we are required to make recommendations setting out:

- Our judgement on the nature of the weakness identified;
- The evidence on which our view is based;
- The impact on the local body; and
- The action the body needs to take to address the weakness.



Value for Money arrangements

Risks of significant weakness in VFM arrangements

We have carried out an initial risk assessment to identify any risks of significant weakness in respect of the three specific areas of proper arrangements using the guidance contained in AGN 03. A significant weakness is a risk requiring audit consideration and procedures to address the likelihood that proper arrangements are not in place at the body to deliver value for money.

We will re-evaluate this risk assessment during the course of the audit and, where appropriate, update our work to reflect emerging risks or findings that may suggest a significant weakness in arrangements.

When considering the Council's arrangements, we will have regard to the three reporting criteria set out in AGN03, as well as performing additional work in the areas identified below which are the potential areas of significant weaknesses, we have identified at the planning stage.

Criteria	Risk of significant weakness	Our risk based procedures and evaluation approach includes (but is not limited to)
Financial sustainability	None identified	<p>Whilst we have not identified, at this stage, any risks of significant weakness, we will consider as part of our review the arrangements in place to monitor and mitigate the commercial, economic and other risks relating to the Council's significant capital schemes and in particular the impact of scope downgrades where insufficient funds are available to complete the schemes as intended.</p> <p>We will also assess the governance arrangements in place in respect of these schemes and the wider transformation ambitions of the Council.</p>
Governance	None identified	
Improving economy, efficiency and effectiveness	None identified	

Weaknesses or risks identified by auditors are only those which have come to their attention during their normal audit work in accordance with the Code of Audit Practice and may not be all that exist.

Audit team and logistics

Your audit team

Role	Name	Contact details
Key Audit Partner	Paul Grady	Paul.grady@azets.co.uk
Engagement Manager	Martha Charima	Martha.Charima@azets.co.uk
In-charge auditor	Ava Campbell	Ava.Campbell@azets.co.uk

Timetable

Event	Date
Planning and risk assessment	Oct – Nov 2023
Reporting of plan to Audit Committee	Nov 2023
Interim audit	Mar 2024
Year end audit	Sep – Oct 2024
Reporting of Audit Findings (ISA260)	Nov 2024
Auditor's Annual Report (AAR)	Nov 2024
Target date of approval of accounts	Nov 2024
Accounts publication deadline (as specified in the Accounts and Audit Regulations 2015)	TBC (likely 30 November 2024)

Our expectations and requirements

For us to be able to deliver the audit in line with the agreed fee and timetable, we require the following:

- Draft financial statements to be produced to a good quality by the deadlines you have agreed with us. These should be complete including all notes, the Narrative Statement and the Annual Governance Statement;
- The provision of good quality working papers at the same time as the draft financial statements. These will be discussed with you in advance to ensure clarity over our expectations;
- The provision of agreed data reports at the start of the audit, fully reconciled to the values in the accounts, to facilitate our selection of samples for testing;
- Ensuring staff are available and on site (as agreed) during the period of the audit;
- Prompt and sufficient responses to audit queries within two working days (unless otherwise agreed) to minimise delays.

The audit process is underpinned by effective project management to ensure that we co-ordinate and apply our resources efficiently to meet your deadlines. It is therefore essential that the audit team and the Council's finance team work closely together to achieve this timetable.

Please note that we will be unable to complete our 2023/24 audit until your audits for all previous financial years have been completed by your predecessor auditors and auditor's reports covering both the financial statements audit and value for money work have been issued. The National Audit Office continues to explore ways to escalate the timely completion of all outstanding local government audits.

Independence, objectivity and other services provided

Auditor independence

We confirm that we comply with the Financial Reporting Council's (FRC) Ethical Standard and are able to issue an objective opinion on the financial statements. We have also complied with the NAOs Auditor Guidance Note 01, issued in September 2022, which contains supplementary guidance on ethical requirements for auditors of local public bodies. We have considered our integrity, independence and objectivity in respect of audit services provided and we do not believe that there are any significant threats or matters which should be brought to your attention, other than the matter on the following page.

Other services

We have detailed in the table below any other services provided to the Council (and the Group), the threats to our independence these present and the safeguards we have put in place to mitigate these threats.

Service	Provided to	Fee	Threats identified and safeguards to mitigate threats to independence
Audit related: Certification of Housing Benefit Assurance Process (HBAP) claim (2023/24)	Council	£28,000 plus per diem rate for additional work required	Self-interest: Given this is likely to be a recurring fee, we consider a threat present. However, the fee is not significant to Azets Audit Services or East Hertfordshire District Council. The fee is fixed (apart from an additional £2,000 for each additional 40+ workbook) and not contingent in nature. Self-review: Whilst housing benefit revenue and expenditure streams are within the financial statements, we do not complete the claim form. The focus of our work is solely testing the data in the claim form prepared by the management. Management: As above, the claim form is completed by management and any adjustments or amendments identified to the form during the certification work are discussed and agreed by management prior to submission of the certification report. We therefore consider these risks sufficiently mitigated.

Independence, objectivity and other services provided

Auditor independence – matter arising

As part of our regular conflict checking procedures, the following potential conflict was identified from an associate in our team who does not work within public sector or commercial audit. The individual works in our Audit and Business Advisory Services (ABAS) team:

“I have a conflict check for the East Hertfordshire Council audit. My mum was a councillor and portfolio holder within the council until May when she gave up her seat and I assume this falls within the financial year being audited.”

This is covered by para 2.55 of the Ethical Standard which states: *‘Where a partner or member of staff of the firm, but who is not a covered person, becomes aware that a person closely associated with them, or a close family member, holds a position described in paragraph 2.53, that individual shall report that fact to the engagement partner, who shall evaluate whether the relationship would compromise independence. If the engagement partner concludes that independence may be compromised, they shall consult with the Ethics Partner/Function to determine whether appropriate safeguards exist. If no such safeguards exist, the firm shall withdraw from the engagement.’*

As a firm we have considered this conflict and concluded it is fully mitigated and adequate safeguards exist, as noted below:

- Our first year of audit is 2023/24 so this individual’s mother was a Councillor for only 6-7 weeks of the first audit year
- The conflict ceased as of the local government elections in May 2023, and therefore ceased 6-7 weeks into the audit appointment
- Audit appointments are made completely independently of the Council – by PSAA – meaning that there was no way the individual could have influenced our appointment
- There are safeguards in place in that the individual concerned will not work on the audit (and has had no involvement to the audit to date), in public sector work as a whole, and has no access to the audit files. He does not fall under public sector supervision or line management and is otherwise wholly unconnected to the public sector team

We have discussed this matter with PSAA who agree that this does not represent an unmitigated conflict with the audit and agreed the safeguards detailed above are sufficient to mitigate any perceived risk.

Accordingly, Azets is content that adequate safeguards exist to fully mitigate the conflict

PSAA set a fee scale for each audit that assumes the audited body has sound governance arrangements in place, has been operating effectively throughout the year, prepares comprehensive and accurate draft accounts and meets the agreed timetable for audit. This fee scale is reviewed by PSAA each year and adjusted, if necessary, based on auditors' experience, new requirements, or significant changes to the audited body. The fee may be varied above the fee scale to reflect the circumstances and local risks within the audited body.

Our estimated fee (excluding VAT) is as follows:

Audit fee	2023/24 £
Base fee for the audit of the Council (and Group's) financial statements (as set out in the fee scales issued by PSAA)	165,497
New auditing standards: ISA315 and ISA240	24,825
Transfer of data to new financial ledger	18,500
Initial audit fee for East Hertfordshire District Council	208,822
Additional work arising from prior year audit outcomes	TBC
Proposed audit fee for East Hertfordshire District Council	TBC

This fee is estimated based on our understanding at this point in time and may be subject to change. Our planned fee is on the basis that our expectations set out on page 17 are met and your group structure is unchanged.

It is our policy to bill for overruns or scope extensions e.g., where we have incurred delays, deliverables have been late or of poor quality, where key personnel have not been available, or we have been asked to do extra work.

Our policy is to raise fees to account at appropriate stages of the audit such as during the audit planning, the interim visit, the final audit and once the financial statements have been signed.

The approximate total fees charged to the Council and group for the provision of services in 2023/24 is as follows:

Audit fee	2023/24 £
Audit of the Council (as above, excluding any additional work arising from prior year audit completion)	208,822
Certification of the HBAP Claim (excluding the per diem rate for additional workbooks)	28,000
Total fees for the Group (excluding any additional work arising from prior year audit completion, and any additional work on the HBAP claim)	236,822

Appendix I: Materiality

Whilst our audit procedures are designed to identify misstatements which are material to our audit opinion, we also report to those charged with governance and management any uncorrected misstatements of lower value errors to the extent that our audit identifies these. Under ISA (UK) 260 we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA (UK) 260 defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

An omission or misstatement is regarded as material if it would reasonably influence the users of the financial statements. The assessment of what is material is a matter of professional judgement and is affected by our assessment of the risk profile of the Council and group and the needs of the users. When planning, we make judgements about the size of misstatements which we consider to be material, and which provide a basis for determining the nature and extent of our audit procedures. Materiality is revised as our audit progresses, should we become aware of any information that would have caused us to determine a different amount had we known about it during our planning.

Our assessment, at the planning stage, of materiality for the year ended 31 March 2024 was calculated as follows:

	Group £'000	Council £'000	Explanation
Overall materiality for the financial statements	1,450	1,350	2% of gross revenue expenditure based on the draft financial statements as at 31 March 2021. This will be reassessed upon receipt of the draft accounts. The financial statements are considered to be materially misstated where total errors exceed this value.
Performance materiality	870	810	60% of materiality. Audit work will be performed to capture individual errors at this level
Trivial threshold	72.5	67.5	5% of overall materiality for the Council and group. Individual errors above this threshold are communicated to those charged with governance.

In addition to the above, we consider any areas for specific lower materiality. We have determined that no specific materiality levels need to be set for this audit.

Appendix II: Group audit scope and risk assessment

As Group auditor under ISA (UK) 600 (Revised November 2019) we are required to obtain sufficient appropriate audit evidence regarding the financial information of the components and the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Please note the below scope is indicative subject to our detailed review of the Council's proposed accounting treatment for the group structure.

Group audit scope

The Group consists of the following entities:

Component	Significant?	Level of response required	Planned audit approach
East Hertfordshire District Council	Yes	Comprehensive	Full scope statutory audit
Millstream Property Investments Ltd	No	Analytical	We will carry out analytical procedures at a group level

Comprehensive The component is of such significance to the Group as a whole that an audit of the components financial statements is required for group reporting purposes.

Targeted The component is significant to the Group, audit evidence will be obtained by performing targeted audit procedures rather than a full audit.

Analytical The component is not significant to the Group and audit risks can be addressed sufficiently by applying analytical procedures at the Group level.

Risks at the component-level

The risks identified at the Council are set out in this external audit plan. There are no other risks identified in any of the other components above in respect of the Group audit.

Note that a component may require a statutory audit under UK or overseas company law irrespective of whether an audit is required for group reporting purposes. Management should therefore satisfy themselves that all UK and overseas company law requirements are adhered to on a company-by-company basis.

Involvement in the work of component auditors

The nature, timing and extent of our involvement in the work of component auditors will begin with a discussion on risks, guidance on designing procedures, participation in meetings, followed by the review of relevant aspects of the audit documentation and meeting with appropriate members of the audit team.

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Agenda Item 7

East Herts Council Report

Audit and Governance Committee

Date: 30 January 2024

Report by: Councillor Carl Brittain, Executive Member for Financial Sustainability

Report title: Mid-Year Treasury Management Review 2023/24

Ward(s) affected: None

Summary

- The report contains the Council's Mid-Year Treasury Management Review for 2023/24.

RECOMMENDATIONS FOR AUDIT AND GOVERNANCE COMMITTEE **That:**

(A) Members examine and comment on the Mid-Year Treasury Management Review and Prudential Indicators for 2023/24

1.0 Proposal(s)

1.1 That Members examine and comment on the Mid-Year Treasury Management Review and Prudential Indicators for 2023/24 (**Appendix A**).

2.0 Background

2.1 Treasury management is defined as: 'The management of the Council's investments and cash flows, its banking arrangements, money market and capital transactions; the

effective control of the risks associated with these activities; and the pursuit of optimum returns consistent with the Council's risk management policy for treasury management.

- 2.2 This activity was supported by the council's appointed independent advisors – Arlingclose.
- 2.3 This report has been written in accordance with the requirements of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised 2017).
- 2.4 This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

3.0 Reason

- 3.1 This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2023/24.

4.0 Options

- 4.1 Members can suggest amendments or additions to the Mid-Year Treasury Management Review 2023/24

5.0 Risks

5.1 Risk management is embedded in treasury management operations through the adoption of the CIPFA Treasury Management Code. Credit ratings, other market intelligence and counterparty limits assist to assess and mitigate risk.

6.0 Implications/Consultations

6.1 None.

Community Safety

No

Data Protection

No

Equalities

No

Environmental Sustainability

No

Financial

Yes

The costs of treasury operations, debt management expenses and investment income are included in the 2023/24 Medium Term Financial Plan.

Health and Safety

No

Human Resources

No

Human Rights

No

Legal

The Local Government Act 2003 and supporting regulations requires the Council to 'have regard to' the CIPFA Prudential Code for Capital Finance in Local Authorities 2017 Edition and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Council also has to 'have regard' to the MHCLG's Guidance on Local Government Investments 3rd Edition effective for financial periods commencing on or after 1st April 2018, and to CIPFA's Treasury Management in the Public Services: Code of Practice 2017 Edition and Guidance Notes for Local Authorities 2018 Edition.

Specific Wards

No

7.0 Background papers, appendices and other relevant material

7.1 Appendix A – Mid-Year Treasury Management Review 2023-24

Contact Member

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Treasury Management Mid-Year Review 2023/24

Introduction

In March 2021 the Authority adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice* (the CIPFA Code) which requires the Authority to approve, as a minimum, treasury management semi-annual and annual outturn reports.

The Authority's treasury management strategy for 2023/24 was approved at a meeting on 1st March 2024. The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Authority's treasury management strategy.

External Context

Economic background: UK inflation remained stubbornly high over much the period compared to the US and euro zone, keeping expectations elevated of how much further the Bank of England (BoE) would hike rates compared to the regions. However, inflation data published in the latter part of the period undershot expectations, causing financial markets to reassess the peak in BoE Bank Rate. This was followed very soon after by the BoE deciding to keep Bank Rate on hold at 5.25% in September, against expectation for another 0.25% rise.

Economic growth in the UK remained relatively weak over the period. In calendar Q2 2023, the economy expanded by 0.2%. However, monthly GDP data showed a 0.5% contraction in July, the largest fall to date in 2023 and worse than the 0.2% decline predicted which could be an indication the monetary tightening cycle is starting to cause recessionary or at the very least stagnating economic conditions.

July data showed the unemployment rate increased to 4.3% (3mth/year) while the employment rate rose to 75.5%. Pay growth was 8.5% for total pay (including bonuses) and 7.8% for regular pay, which for the latter was the highest recorded annual growth rate. Adjusting for inflation, pay growth in real terms were positive at 1.2% and 0.6% for total pay and regular pay respectively.

Inflation continued to fall from its peak as annual headline CPI declined to 6.7% in July 2023 from 6.8% in the previous month against expectations for a tick back up to 7.0%. The largest downward contribution came from food prices. The core rate also surprised on the downside, falling to 6.2% from 6.9% compared to predictions for it to only edge down to 6.8%.

The Bank of England's Monetary Policy Committee continued tightening monetary policy over most of the period, taking Bank Rate to 5.25% in August. Against expectations of a further hike in September, the Committee voted 5-4 to maintain Bank Rate at 5.25%. Each of the four dissenters were in favour of another 0.25% increase.

Financial market Bank Rate expectations moderated over the period as falling inflation and weakening data gave some indication that higher interest rates were working. Expectations fell from predicting a peak of over 6% in June to 5.5% just ahead of the September MPC meeting, and to then expecting 5.25% to be the peak by the end of the period.

Following the September MPC meeting, Arlingclose, the authority's treasury adviser, modestly revised its interest forecast to reflect the central view that 5.25% will now be the peak in Bank Rate. In the short term the risks are to the upside if inflation increases again, but over the remaining part of the time horizon the risks are to the downside from economic activity weakening more than expected.

The lagged effect of monetary policy together with the staggered fixed term mortgage maturities over the next 12-24 months means the full impact from Bank Rate rises are still yet to be felt by households. As such, while consumer confidence continued to improve over the period, the GfK measure hit -21 in September, it is likely this will reverse at some point. Higher rates will also impact business and according to S&P/CIPS survey data, the UK manufacturing and services sector contracted during the quarter with all measures scoring under 50, indicating contraction in the sectors.

The US Federal Reserve increased its key interest rate to 5.25-5.50% over the period, pausing in September following a 0.25% rise the month before, and indicating that it may have not quite completed its monetary tightening cycle.

Having fallen throughout 2023, annual US inflation started to pick up again in July 2023, rising from 3% in June, which represented the lowest level since March 2021, to 3.2% in July and then jumping again to 3.7% in August, beating expectations for a rise to 3.6%. Rising oil prices were the main cause of the increase. US GDP growth registered 2.1% annualised in the second calendar quarter of 2023, down from the initial estimate of 2.4% but above the 2% expansion seen in the first quarter.

The European Central Bank increased its key deposit, main refinancing, and marginal lending interest rates to 4.00%, 4.50% and 4.75% respectively in September, and hinted these levels may represent the peak in rates but also emphasising rates would stay high for as long as required to bring inflation down to target.

Although continuing to decline steadily, inflation has been sticky, Eurozone annual headline CPI fell to 5.2% in August while annual core inflation eased to 5.3% having stuck at 5.5% in the previous two months. GDP growth remains weak, with recent data showing the region expanded by only 0.1% in the three months to June 2023, the rate as the previous quarter.

Financial markets: Financial market sentiment and bond yields remained volatile, with the latter generally trending downwards as there were signs inflation, while still high, was moderating and interest rates were at a peak.

Gilt yields fell towards the end of the period. The 5-year UK benchmark gilt yield rose from 3.30% to peak at 4.91% in July before trending downwards to 4.29%, the 10-year gilt yield rose from 3.43% to 4.75% in August before declining to 4.45%, and the 20-year yield from 3.75% to 4.97% in August and then fell back to 4.84%. The Sterling Overnight Rate (SONIA) averaged 4.73% over the period.

Credit review: Having completed a review of its credit advice on unsecured deposits at UK and non-UK banks following concerns of a wider financial crisis after the collapse of Silicon Valley Bank purchase of Credit Suisse by UBS, as well as other well-publicised banking sector issues, in March Arlingclose reduced the advised maximum duration limit for all banks on its recommended counterparty list to 35 days. This stance continued to be maintained at the end of the period.

During the second quarter of the period, Moody's revised the outlook on Svenska Handelsbanken to negative from stable, citing concerns around the Swedish real estate sector.

Having put the US sovereign rating on Rating Watch Negative earlier in the period, Fitch took further action in August, downgrading the long-term rating to AA+, partly around ongoing debt ceiling concerns but also an expected fiscal deterioration over the next couple of years.

Following the issue of a Section 114 notice, in September Arlingclose advised against undertaking new lending to Birmingham City Council, and later in the month cut its recommended duration on Warrington Borough Council to a maximum of 100 days.

Arlingclose continued to monitor and assess credit default swap levels for signs of ongoing credit stress and although no changes were made to recommended durations over the period, Northern Trust Corporation was added to the counterparty list.

Heightened market volatility is expected to remain a feature, at least in the near term and, as ever, the institutions and durations on the Authority's counterparty list recommended by Arlingclose remains under constant review.

Local Context

On 31st March 2023, the Authority had net investments of £15.073m arising from its revenue and capital income and expenditure. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying resources available for investment. These factors are summarised in Table 1 below.

Table 1: Balance Sheet Summary

	31.3.23 Actual £m	31.3.24 Forecast £m
General Fund CFR	40.071	56.681
Less: *Other debt liabilities	-	-
External borrowing**	31.500	47.742
Internal borrowing	8.571	8.939
Less: Balance sheet resources	(23.644)	(23.644)
Net investments	15.073	14.705

* finance leases, PFI liabilities and transferred debt that form part of the Authority's total debt

** shows only loans to which the Authority is committed and excludes optional refinancing

The treasury management position at 30th September and the change over the six months' is shown in Table 2 below.

Table 2: Treasury Management Summary

	31.3.23 Balance £m	Movement £m	30.9.23 Balance £m	30.9.23 Rate %
Long-term borrowing				
- PWLB	(1.5)	-	(1.5)	8.875
- LOBOs	-	-	-	-
- Other	-	-	-	-
Short-term borrowing	(30.0)	(5.0)	(35.0)	4.03
Total borrowing	(31.5)	(5.0)	(36.5)	-
Long-term investments	19.5	(0.6)	18.9	3.42
Short-term investments	6.5	(0.5)	6.0	5.16
Cash and cash equivalents	4.3	0.7	5.0	4.78
Total investments	30.3	(0.4)	29.9	-
Net borrowing	(1.2)	(5.4)	(6.6)	-

Borrowing

CIPFA's 2021 Prudential Code is clear that local authorities must not borrow to invest primarily for financial return and that it is not prudent for local authorities to make any investment or spending decision that will increase the capital financing requirement and so may lead to new borrowing, unless directly and primarily related to the functions of the Authority. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield unless these loans are for refinancing purposes.

The Authority has reviewed its capital programme in light of the Prudential Code 2021 requirements and PWLB lending arrangements to ensure that borrowing to invest primarily for commercial return is no longer undertaken.

Borrowing strategy and activity

As outlined in the treasury strategy, the Authority's chief objective when borrowing has been to strike an appropriately low risk balance between securing lower interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Authority's long-term plans change being a secondary objective. The Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.

There was a substantial rise in the cost of both short - and long-term borrowing over the last 18 months. Bank Rate rose by 1% from 4.25% at the beginning of April to 5.25% at the end of September. Bank Rate was 2% higher than at the end of September 2022.

UK gilt yields were volatile, mainly facing upward pressure since early April following signs that UK growth had been more resilient, inflation stickier than expected, and that the Bank of England saw persistently higher rates through 2023/24 as key to dampening domestic demand. Gilt yields, and consequently PWLB borrowing rates, rose and broadly remained at elevated levels. On 30th September, the PWLB certainty rates for maturity loans were 5.26% for 10-year loans, 5.64% for 20-year loans and 5.43% for 50-year loans. Their equivalents on 31st March 2023 were 4.33%, 4.70% and 4.41% respectively.

At 30th September the Authority held £36.5m of loans, (an increase of £5m compared to 31st March 2023), as part of its strategy for funding previous and current years' capital programmes. Outstanding loans on 30th September are summarised in Table 3 below.

Table 3: Borrowing Position

	31.3.23 Balance £m	Net Movement £m	30.9.23 Balance £m	30.9.23 Weighted Average Rate %	30.9.23 Weighted Average Maturity (years)
Public Works Loan Board	1.5	0.0	1.5	8.875	31
Banks (LOBO)	-	-	-	-	-
Banks (fixed-term)	-	-	-	-	-
Local authorities (long-term)	-	-	-	-	-
Local authorities (short-term)	30	5	35	4.030	<1
Total borrowing	31.5	5	31.5	-	-

The Authority's short-term borrowing cost has continued to increase with the rise in Bank Rate and short-dated market rates. The average rate on the Authority's short-term loans at 30th September 2023 of was 4.030%, this compares with 2.256% on £30m loans 6 months ago.

The Authority's borrowing decisions are not predicated on any one outcome for interest rates and a balanced portfolio of short and long-term borrowing was maintained.

Forward starting loans: To enable certainty of cost to be achieved without suffering a cost of carry in the intervening period, the Authority arranged the above Local authority (short-term) loans as forward starting loans with fixed interest rates. This resulted in interest rate savings.

There remains a strong argument for diversifying funding sources, particularly if rates can be achieved on alternatives which are below gilt yields + 0.80%. The Authority will evaluate and pursue these lower cost solutions and opportunities with its advisor Arlingclose.

Debt Rescheduling: No debt rescheduling has been undertaken to date in the current financial year.

Treasury Investment Activity

The CIPFA Treasury Management Code now defines treasury management investments as those investments which arise from the Authority's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business.

The Authority holds invested funds, representing income received in advance of expenditure plus balances and reserves held. During the half year, the Authority's investment balances ranged between £11 and £19 million due to timing differences between income and expenditure. The investment position is shown in table 4 below.

Table 4: Treasury Investment Position

	31.3.23 Balance £m	Net Movement £m	30.9.23 Balance £m	30.9.23 Income Return %
Banks & building societies	8.2	(4.8)	3.4	4.4
Covered bonds (secured)	-	-	-	-
Government	-	-	-	-
Local authorities and other govt entities	-	5.0	5	5.3
Corporate bonds and loans	-	-	-	-
Money Market Funds	2.6	-	2.6	5.2
Property Funds	19.5	(0.6)	18.9	3.4
Total investments	30.3	(0.4)	29.9	-

Both the CIPFA Code and government guidance require the Authority to invest its funds prudently, and to have regard to the security and liquidity of its treasury investments before seeking the optimum rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

As demonstrated by the liability benchmark in this report, the Authority expects to be a long-term borrower and new treasury investments are therefore primarily made to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different asset classes and boost investment income.

Bank Rate increased by 1%, from 4.25% at the beginning of April to 5.25% by the end of September. Short-dated cash rates rose commensurately, with 3-month rates rising to around 5.25% and 12-month rates to nearly 6%. The rates on DMADF deposits also rose, ranging between 4.8% and 5.4% by the end of June and Money Market Rates between 4.08% and 5.26%.

£18.9m that is available for longer-term investment invested in property funds, have produced significantly higher returns than other investments in previous years, however these returns and fund value have dipped due to the current climate. We are currently in the process of drawing down on these funds.

Financial market conditions were volatile during the six-month period. Global bond yields rose and remained elevated as it became apparent that policymakers were looking to keep rates high for some time amid persistently higher core inflation and tight labour markets.

The UK, Euro area and US equity markets were initially helped by resilient growth data and diminishing talk of recession. A weaker currency and better-than-expected fundamentals were broadly supportive for UK equities. Much of the US stock market's performance was driven by a small number of mega stocks and enthusiasm over artificial intelligence. However the global outlook was clouded by the slowdown in China. On a sectoral level, the energy sector was supported by higher oil prices and expectation of decreasing supply due to OPEC+ group agreeing on production cuts. The FTSE All Share index was marginally lower at the end of the 6-month period at 4127 on 30/9/23 v 4157 on 31/3/23. The MSCI All Countries World Index was higher at 2853 on 30/9/23 v 2791 on 31/3/23.

For existing longer-term investors in fixed income securities, the prospect of a higher-for-longer rate environment weighed on sentiment. Yields rose in Q2 2023 on the expectation that central banks would continue hiking rates but fell in August as investors grew confident that policy rates were close to their peak, then rose again in September as oil prices climbed above \$90/barrel. There was also some effect from quantitative tightening by the Bank of England.

Investor sentiment for UK commercial property was more settled than in Q3 and Q4 of 2022 when the sharp rise in bond yields resulted in a big fall in property valuations. There were signs of returning investor interest, occupier resilience and a perception that the downturn in commercial real estate may be bottoming out. It helped rental income and led to some stabilisation in capital values. However, the combination of high interest rates and bond yield, higher funding costs and the prospect of sluggish economic growth constrain the outlook for commercial property.

The combination of the above had a negative effect on the combined value of the Authority's strategic funds since March 2023. Income from the Authority's cash has improved as maturing securities are replaced by higher yielding ones in these funds.

The change in the Authority's funds' capital values and income return over the 6-month period is shown in Table 4.

Income returns have dropped to an average 3.4%. The Authority has budgeted £800,000 gross income from these investments in 2023/24. Gross income received up to 30th September was £412,000.

Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority’s medium- to long-term investment objectives are regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down on months, quarters and even years; but with the confidence that over a three- to five-year minimum period total returns will exceed cash interest rates.

Statutory override: In April 2023 the Department for Levelling Up, Housing and Communities published the full outcome of the consultation on the extension of the statutory override on accounting for gains and losses on pooled investment funds. The override has been extended for two years until 31st March 2025 but no other changes have been made; whether the override will be extended beyond the new date is unknown but commentary to the consultation outcome suggests not. The Authority will discuss with Arlingclose the implications for the investment strategy and what action may need to be taken.

Non-Treasury Investments

The definition of investments in the Treasury Management Code now covers all the financial assets of the Authority as well as other non-financial assets which the Authority holds primarily for financial return. Investments that do not meet the definition of treasury management investments (i.e. management of surplus cash) are categorised as either for service purposes (made explicitly to further service objectives) and or for commercial purposes (made primarily for financial return).

Investment Guidance issued by the Department for Levelling Up Housing and Communities (DLUHC) and Welsh Government also includes within the definition of investments all such assets held partially or wholly for financial return.

The Authority also held £13.6m of such investments in

- directly owned property £8.6m
- shareholding in subsidiaries £4.9m
- loans to subsidiaries £0.1m

Compliance

The Head of Strategic Finance and property reports that all treasury management activities undertaken during the quarter complied fully with the principles in the Treasury Management Code and the Authority’s approved Treasury Management Strategy.

Compliance with the Authorised Limit and Operational Boundary for external debt is demonstrated in table 8 below.

Table 5: Debt and the Authorised Limit and Operational Boundary

	30.9.23 Actual	2023/24 Operational Boundary £m	2023/24 Authorised Limit £m	Complied? Yes/No
Borrowing	36.5	80.0	180.0	Yes
PFI and Finance Leases	-	10.0	10.0	Yes
Total debt	36.5	90.0	190.0	Yes

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

Treasury Management Prudential Indicators

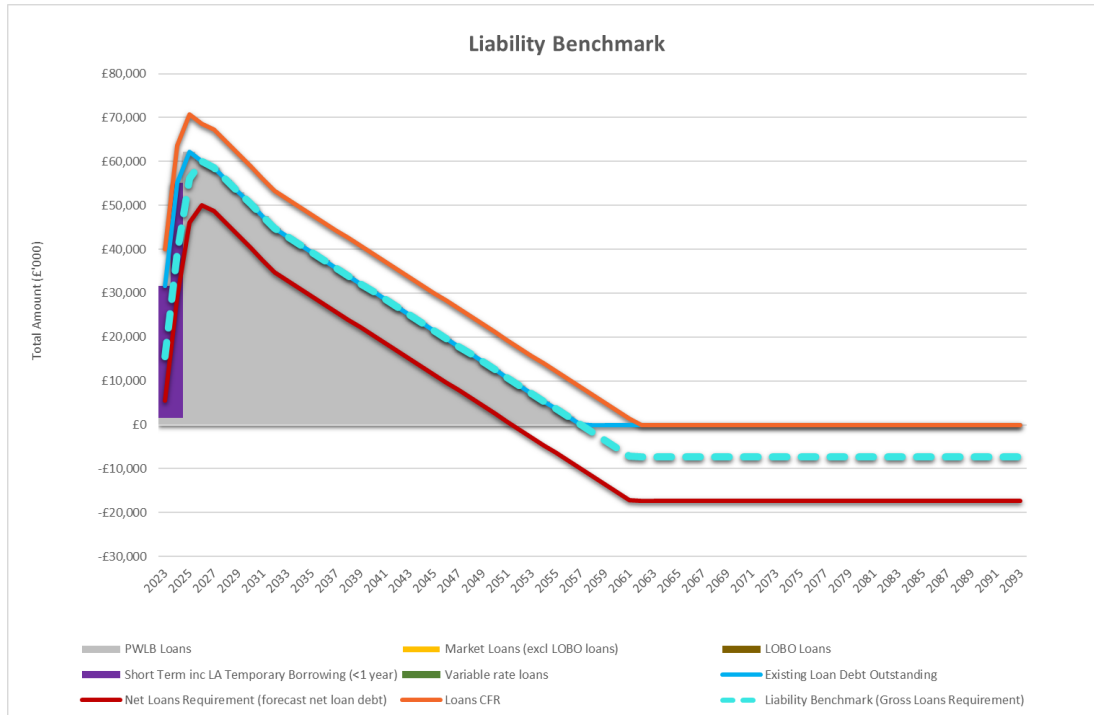
As required by the 2021 CIPFA Treasury Management Code, the Authority monitors and measures the following treasury management prudential indicators.

1. Liability Benchmark:

This new indicator compares the Authority's actual existing borrowing against a liability benchmark that has been calculated to show the lowest risk level of borrowing. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. It represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level of £10m required to manage day-to-day cash flow.

	31.3.23 Actual £'000	31.3.24 Forecast £'000	31.3.25 Forecast £'000	31.3.26 Forecast £'000
Loans CFR	40.071	63.699	70.720	68.570
Less: Balance sheet resources	(34.574)	(34.574)	(24.574)	(18.573)
Net loans requirement	5.497	29.125	46.146	49.997
Plus: Liquidity allowance	10.000	10.000	10.000	10.000
Liability benchmark	15.497	39.125	56.146	59.997
Existing borrowing	30.000	45.000	60.000	63.000

Following on from the medium-term forecast above, the long-term liability benchmark assumes capital expenditure funded by borrowing of £63m a year, minimum revenue provision on new capital expenditure based on a 30 year asset life and income, expenditure and reserves all increasing by inflation of 2% a year. This is shown in the chart below together with the maturity profile of the Authority's existing borrowing.



Whilst borrowing may be above the liability benchmark, strategies involving borrowing which is significantly above the liability benchmark carry higher risk.

2. **Maturity Structure of Borrowing:** This indicator is set to control the Authority’s exposure to refinancing risk. The upper and lower limits on the maturity structure of all borrowing were:

	Upper Limit	Lower Limit	30.9.23 Actual	Complied?
Under 12 months	100%	0%	95.89%	Yes
12 months and within 24 months	100%	0%	0%	Yes
24 months and within 5 years	30%	0%	0%	Yes
5 years and within 10 years	30%	0%	0%	Yes
10 years and above (35%	0%	4.11%	Yes

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

3. **Long-term Treasury Management Investments:** The purpose of this indicator is to control the Authority’s exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management limits are:

	2023/24	2024/25	2025/26
Limit on principal invested beyond year end	£30m	£30m	£30]m
Actual principal invested beyond year end	£20m	-	-
Complied?	Yes	-	-

Long-term investments with no fixed maturity date include strategic pooled funds, real estate investment trusts and directly held equity but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

Additional information:

The changes in interest rates during the quarter were:

	<u>31/3/23</u>	<u>30/9/23</u>
Bank Rate	4.25%	5.25%
1-year PWLB certainty rate, maturity loans	4.78%	5.69%
5-year PWLB certainty rate, maturity loans	4.31%	5.22%
10-year PWLB certainty rate, maturity loans	4.33%	5.26%
20-year PWLB certainty rate, maturity loans	4.70%	5.64%
50-year PWLB certainty rate, maturity loans	4.41%	5.43%

East Herts Council Report

Audit and Governance Committee

Date: 30th January 2024

Report by: Councillor Carl Brittain, Executive Member for Financial Sustainability

Report title: Capital Strategy and Minimum Revenue Provision Policy, Treasury Management Strategy 2024/25

Ward(s) affected: All

Summary

- The report contains the Capital Strategy and Minimum Revenue Provision (MRP) policy and Treasury Management Strategy for 2024/25 for Scrutiny

RECOMMENDATIONS FOR AUDIT AND GOVERNANCE:

(A) Scrutinise the Capital Strategy and Minimum Revenue Provision Policy, Treasury Management Strategy 2024/25 and make any observations to the Executive.

1.0 Proposal(s)

1.1 This report presents the Executive's Capital Strategy and the Minimum Revenue Provision policy and Treasury Management Strategy 2024/25 onwards for Scrutiny.

2.0 Background

- 2.1 The East Herts Council Capital Strategy provides a valuable opportunity for engagement with Full Council to ensure that overall strategy, investment ambition, risk appetite and governance procedures are fully understood by all elected Members and other Council stakeholders.
- 2.2 The East Herts Council Capital Strategy is intended to be a strategic corporate document which will both be influenced by and in turn influence policy and decision making in respect of capital investment.
- 2.3 The Strategy will continue to develop and evolve as external influences do and will be updated as required in order that this Strategy is responsive to the challenges, opportunities, priorities and objectives that the Council must consider.
- 2.4 The current capital programme pauses the Arts Centre at Old River Lane in order to make the capital programme affordable by reducing borrowing costs.
- 2.5 As the council continues to deliver, review and update the capital programme, it will do so within the context of the council's Climate Change commitments, most notably the commitment to the council itself becoming carbon neutral by 2030. To that end, the council has devised a carbon assessment tool which it is now beginning to use to assess its existing major projects. As new proposals for capital funding come forward, a carbon assessment will be included as an integral part of the business case to inform decision-making.
- 2.6 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to

ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with the Council's low risk appetite, providing security and adequate liquidity always before considering investment return.

- 2.7 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans, or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.
- 2.8 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.
- 2.9 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities.

- 2.10 This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).
- 2.11 This activity is currently supported by the council's appointed independent advisors – Link Asset Services.
- 2.12 The strategy was scrutinised by Audit and Governance Committee at its meeting on 24 January 2023 and made no comments

3.0 Reason(s)

- 3.1 Revised reporting was required from the 2019/20 reporting cycle due to revisions of the MHCLG Investment Guidance, the MHCLG Minimum Revenue Provision (MRP) Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code. The primary reporting changes included the introduction of a capital strategy, to provide a longer-term focus to the capital plans, and greater reporting requirements surrounding any commercial activity undertaken under the Localism Act 2011.
- 3.2 This report includes the fourth capital strategy since the revisions. The first three versions of the report were welcomed by Members and no comments or suggestions for improvement have been received from either internal or external audit.

4.0 Options

- 4.1 Endorse the updated strategy or suggest amendments because of the scrutiny process.

5.0 Risks

5.1 Risks are discussed in detail, within the Capital Strategy, including the uncertainty around future funding.

6.0 Implications/Consultations

6.1 None

Community Safety

Building and refurbishment schemes design out crime and safety issues and public realm works in particular are required to ensure that the community feel safe.

Data Protection

All investment in IT systems are required to check where data is held and that systems comply with data protection legislation.

Equalities

All capital schemes meet the necessary legislation and are subject to access audits. Design also takes into account dementia friendly design elements particularly around colour.

Environmental Sustainability

The council has established a carbon assessment tool that it is beginning to apply to existing capital projects. In the future, a carbon assessment of proposed capital projects will be included within the overall business case so as to inform decision-making. To date, individual schemes have sustainability features designed into them and may include, for example: meeting BREEAM ratings for buildings and refurbishments; flood resilience and sustainable underground drainage systems; opportunities for renewable energy generation; and carbon reduction such as replacement of the council's internal combustion engine vehicles with battery electric vehicles.

Financial

The strategy guides the capital programme and detailed financial implications are included with that in the budget report

Health and Safety

All contractors are required to have compliant health and safety policies. Where a health and safety issue requires capital expenditure it will be fast tracked to deal with the issue

Human Resources

None

Human Rights

None

Legal

A Capital Strategy is a requirement of the Prudential Code which the council is required to follow under the Local Government Act 2003.

Specific Wards

None

7.0 Background papers, appendices and other relevant material

7.1 **Appendix A** - East Herts District Council Draft Capital Strategy and Minimum Revenue Policy 2023/24 Onwards

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Capital Strategy

2024/25

Including Minimum Revenue Provision
Policy

2.1. Capital Expenditure *Table 1: Prudential Indicator: Estimates of Capital Expenditure*

	2022/23 actual £(000)	2023/24 forecast £(000)	2024/25 budget * £(000)	2025/26 budget £(000)	2026/27 budget £(000)
General Fund services	15,430	31,322	16,437	1,452	2,326
Capital investments	-	-	-	-	-
TOTAL	15,430	31,322	16,437	1,452	2,326

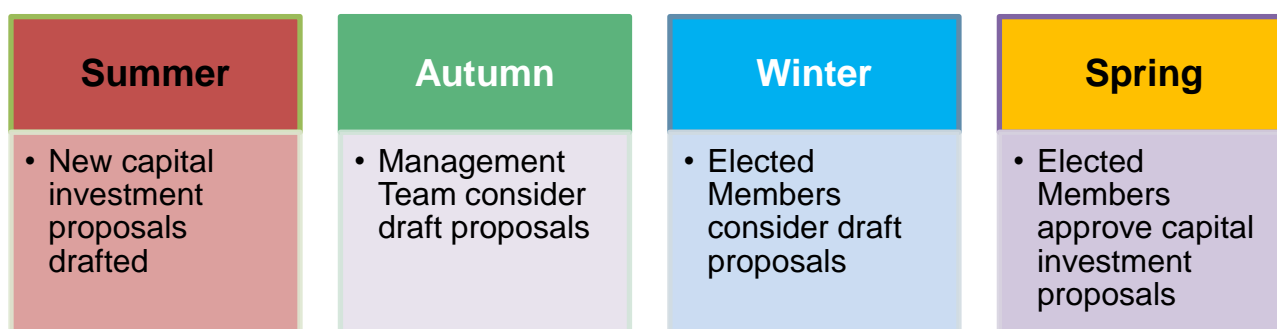


Table 2: Capital financing

	2022/23 actual £(000)	2023/24 forecast £(000)	2024/25 budget * £(000)	2025/26 budget £(000)	2026/27 budget £(000)
External sources	2,207	3,506	83	-	-
Capital receipts	1,427	306	250	250	250
Revenue resources	53	3,288	2,051	650	650
Debt	11,743	24,222	14,053	552	1,426
TOTAL	15,430	31,322	16,437	1,452	2,326

Table 3: Replacement of prior years' debt finance

	2022/23 actual £(000)	2023/24 forecast £(000)	2024/25 budget £(000)	2025/26 budget £(000)	2026/27 budget £(000)
Minimum revenue provision (MRP)	0	594	1,032	2,701	2,786
Capital receipts	0	-	6,000	-	-
TOTAL	0	594	7,032	2,701	2,786

Table 4: Capital Financing Requirement (CFR)

	2022/23 actual £(000)	2023/24 forecast £(000)	2024/25 budget £(000)	2025/26 budget £(000)	2026/27 budget £(000)
Capital Financing Requirement (CFR)	40,071	63,699	70,720	68,570	67,210

3.6.1. To ensure that capital assets continue to be of long-term use, the Authority has an asset management strategy in place. The council's assets are being reviewed to identify assets for disposal to repay borrowing. The council is exploring transferring parks, open spaces, playing fields, playgrounds, grass verges and woodland to Town and Parish Councils. Ware Town Council has come forward with a desire to transfer assets and we are working with them to develop this policy.

Asset Disposals Table 5: Capital receipts receivable

	2022/23 actual £(000)	2023/24 forecast £(000)	2024/25 budget £(000)	2025/26 budget £(000)	2026/27 budget £(000)
Asset sales	1,177	3,256	6,000	-	-
Preserved Right to Buy Receipts	250	250	250	250	250
Loans etc repaid	-	-	-	-	-
TOTAL	1,427	3,506	6,250	250	250

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement

	31.3.2023 actual £(000)	31.3.2024 forecast £(000)	31.3.2025 budget £(000)	31.3.2026 budget £(000)	31.3.2027 budget £(000)
Debt (incl. PFI & leases)	31,522	55,180	62,827	60,678	59,318
Capital Financing Requirement	40,071	63,699	70,720	68,570	67,210

Table 7: Borrowing and the Liability Benchmark

	31.3.2023 actual £(000)	31.3.2024 forecast £(000)	31.3.2025 budget £(000)	31.3.2026 budget £(000)	31.3.2027 budget £(000)
Forecast borrowing	31,522	55,180	62,827	60,678	59,318
Liability benchmark	15,497	39,125	56,146	59,997	58,637

Table 8: Prudential Indicators: Authorised limit and operational boundary for external debt

	2023/24 limit £(000)	2024/25 limit £(000)	2025/26 limit £(000)	2026/27 limit £(000)
Authorised limit - total external debt	180	150	150	150
Operational boundary - total external debt	90	75	75	75

Table 9: Treasury management investments

	31.3.2023 actual	31.3.2024 forecast	31.3.2025 budget	31.3.2026 budget	31.3.2027 budget
Near-term investments	6,056	6,056	6,056	11,000	11,000
Longer-term investments	19,999	19,999	9,998	-	-
TOTAL	26,055	26,055	16,054	11,000	11,000

Table 11: Prudential Indicator: Proportion of financing costs to net revenue stream

	2022/23 actual	2023/24 forecast	2024/25 budget *	2025/26 budget	2026/27 budget
Financing costs (£m)					
Proportion of net revenue stream	%	%	%	%	%

Annual Minimum Revenue Provision Statement 2024/25

1. Where the Authority finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Authority to have regard to the former Ministry of Housing, Communities and Local Government's Guidance on Minimum Revenue Provision (the MHCLG Guidance) most recently issued in 2018.
2. The broad aim of the MHCLG Guidance is to ensure that capital expenditure is financed over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.
3. The MHCLG Guidance requires the Authority to approve an Annual MRP Statement each year and recommends a number of options for calculating a prudent amount of MRP. The following statement [only] incorporates options recommended in the Guidance.
4. For capital expenditure incurred after 31st March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant asset in equal instalments starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over 20 years.
5. For assets acquired by leases MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.
6. Where former operating leases have been brought onto the balance sheet due to the adoption of the IFRS 16 Leases accounting standard, and the asset values have been adjusted for accruals, prepayments, premiums

and/or incentives, then the annual MRP charges will be adjusted so that the total charge to revenue remains unaffected by the new standard.

7. For capital expenditure loans to third parties, the Authority will make nil MRP unless an expected credit loss was recognised or increased in-year but will instead apply the capital receipts arising from principal repayments to reduce the capital financing requirement instead. Sufficient MRP will be charged to ensure that the outstanding capital financing requirement (CFR) on the loan is no higher than the principal amount outstanding less the expected credit loss. This option was proposed by the government in its recent MRP consultation and in the Authority's view is consistent with the current regulations.
8. Capital expenditure incurred during 2024/25 will not be subject to a MRP charge until 2025/26 or later.
9. Based on the Authority's latest estimate of its capital financing requirement (CFR) on 31st March 2023, the budget for MRP has been set as follows:

	31.03.2024 Estimated CFR £m	2024/25 Estimated MRP £
Capital expenditure		
Leases		
Loans to other bodies repaid in instalments	0	0
Voluntary overpayment	0	0
Total General Fund		

Treasury Management Strategy

2024/25

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Introduction

1. Treasury management is the management of the Authority's cash flows, borrowing and investments, and the associated risks. The Authority has [borrowed and/or invested] substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Authority's prudent financial management.
2. Treasury risk management at the Authority is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2021 Edition (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year. This report fulfils the Authority's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

Economic Background The impact on the UK from higher interest rates and inflation, a weakening economic outlook, an uncertain political climate due to an upcoming general election, together with war in Ukraine and the Middle East, will be major influences on the Authority's treasury management strategy for 2024/25.

4. The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level in September and then again in November. Members of the BoE's Monetary Policy Committee voted 6-3 in favour of keeping Bank Rate at 5.25%. The three dissenters wanted to increase rates by another 0.25%.
5. The November quarterly Monetary Policy Report (MPR) forecast a prolonged period of weak Gross Domestic Product (GDP) growth with the potential for a mild contraction due to ongoing weak economic activity. The outlook for CPI inflation was deemed to be highly uncertain, with near-term risks to CPI falling to the 2% target coming from potential energy price increases, strong domestic wage growth and persistence in price-setting.
6. Office for National Statistics (ONS) figures showed CPI inflation was 6.7% in September 2023, unchanged from the previous month but above the 6.6% expected. Core CPI inflation fell to 6.1% from 6.2%, in line with predictions. Looking ahead, using the interest rate path implied by financial markets the BoE expects CPI inflation to continue falling, declining to around 4% by the end of calendar 2023 but taking until early

2025 to reach the 2% target and then falling below target during the second half 2025 and into 2026.

7. ONS figures showed the UK economy grew by 0.2% between April and June 2023. The BoE forecasts GDP will likely stagnate in Q3 but increase modestly by 0.1% in Q4, a deterioration in the outlook compared to the August MPR. The BoE forecasts that higher interest rates will constrain GDP growth, which will remain weak over the entire forecast horizon.
8. The labour market appears to be loosening, but only very slowly. The unemployment rate rose slightly to 4.2% between June and August 2023, from 4.0% in the previous 3-month period, but the lack of consistency in the data between the two periods made comparisons difficult. Earnings growth remained strong, with regular pay (excluding bonuses) up 7.8% over the period and total pay (including bonuses) up 8.1%. Adjusted for inflation, regular pay was 1.1% and total pay 1.3%. Looking forward, the MPR showed the unemployment rate is expected to be around 4.25% in the second half of calendar 2023, but then rising steadily over the forecast horizon to around 5% in late 2025/early 2026.
9. Having increased its key interest rate to a target range of 5.25-5.50% in August 2023, the US Federal Reserve paused in September and November, maintaining the Fed Funds rate target at this level. It is likely this level represents the peak in US rates, but central bank policymakers emphasised that any additional tightening would be dependent on the cumulative impact of rate rises to date, together with inflation and developments in the economy and financial markets.
10. US GDP grew at an annualised rate of 4.9% between July and September 2023, ahead of expectations for a 4.3% expansion and the 2.1% reading for Q2. But as the impact from higher rates is felt in the coming months, a weakening of economic activity is likely. Annual CPI inflation remained at 3.7% in September after increasing from 3% and 3.2% consecutively in June and July.
11. Eurozone inflation has declined steadily since the start of 2023, falling to an annual rate of 2.9% in October 2023. Economic growth has been weak, and GDP was shown to have contracted by 0.1% in the three months to September 2023. In line with other central banks, the European Central Bank has been increasing rates, taking its deposit facility, fixed rate tender, and marginal lending rates to 3.75%, 4.25% and 4.50% respectively.

Credit outlook

12. Credit Default Swap (CDS) prices were volatile during 2023, spiking in March on the back of banking sector contagion concerns following the major events of Silicon Valley Bank becoming insolvent and the takeover of Credit Suisse by UBS. After then falling back in Q2 of calendar 2023, in the second half of the year, higher interest rates and inflation, the ongoing war in Ukraine, and now the Middle East, have led to CDS prices increasing steadily.
13. On an annual basis, CDS price volatility has so far been lower in 2023 compared to 2022, but this year has seen more of a divergence in prices between ringfenced (retail) and non-ringfenced (investment) banking entities once again.
14. Moody's revised its outlook on the UK sovereign to stable from negative to reflect its view of restored political predictability following the volatility after the 2022 mini-budget. Moody's also affirmed the Aa3 rating in recognition of the UK's economic resilience and strong institutional framework.
15. Following its rating action on the UK sovereign, Moody's revised the outlook on five UK banks to stable from negative and then followed this by the same action on five rated local authorities. However, within the same update the long-term ratings of those five local authorities were downgraded.
16. There remain competing tensions in the banking sector, on one side from higher interest rates boosting net income and profitability against another of a weakening economic outlook and likely recessions that increase the possibility of a deterioration in the quality of banks' assets.
17. However, the institutions on our adviser Arlingclose's counterparty list remain well-capitalised and their counterparty advice on both recommended institutions and maximum duration remain under constant review and will continue to reflect economic conditions and the credit outlook.

Interest rate forecast

18. Although UK inflation and wage growth remain elevated, the Authority's treasury management adviser Arlingclose forecasts that Bank Rate has peaked at 5.25%. The Bank of England's Monetary Policy Committee will cut rates in the medium term to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round

effects. Arlingclose sees rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.

19. Arlingclose expects long-term gilt yields to eventually fall from current levels (amid continued volatility) reflecting the lower medium-term path for Bank Rate. However, yields will remain relatively higher than in the past, due to quantitative tightening and significant bond supply. As ever, there will undoubtedly be short-term volatility due to economic and political uncertainty and events.
20. Like the BoE, the Federal Reserve and other central banks see persistently high policy rates through 2023 and 2024 as key to dampening domestic inflationary pressure. Bond markets will need to absorb significant new supply, particularly from the US government.
21. A more detailed economic and interest rate forecast provided by Arlingclose is in Appendix A.
22. For the purpose of setting the budget, it has been assumed that new treasury investments will be made at an average rate/yield of 5.1%, and that new long-term loans will be avoided with short term borrowing at an average rate of 5%. Based on interest rate forecasts, the short term borrowing will be replaced with long term borrowing during 2026.

Local context

23. On 31st December 2023, the Authority held £31.522m of borrowing and £34.2m of treasury investments. This is set out in further detail at Appendix B. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance sheet summary and forecast

	31.3.23 Actual £(000)	31.3.24 Estimate £(000)	31.3.25 Forecast £(000)	31.3.26 Forecast £(000)	31.3.27 Forecast £(000)
Capital financing requirement	40,071	63,699	70,720	68,570	67,210
Less: Other debt liabilities *	-	-	-	-	-
Loans CFR	40,071	63,699	70,720	68,570	67,210
Less: External borrowing **	31,522	55,180	62,827	60,678	59,318
Internal borrowing	8,549	8,519	7,893	7,892	7,892
Less: Balance sheet resources	34,574	34,574	24,574	18,573	18,573
Treasury investments	26,025	26,025	16,681	10,681	10,681

* leases and PFI liabilities that form part of the Authority's total debt

** shows only loans to which the Authority is committed and excludes optional refinancing

24. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while balance sheet resources are the underlying sums available for investment. The Authority's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.
25. The Authority has an increasing CFR due to the capital programme, but minimal investments and will therefore be required to borrow up to £70.7m over the forecast period.
26. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Authority's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Authority expects to comply with this recommendation during 2024/25.

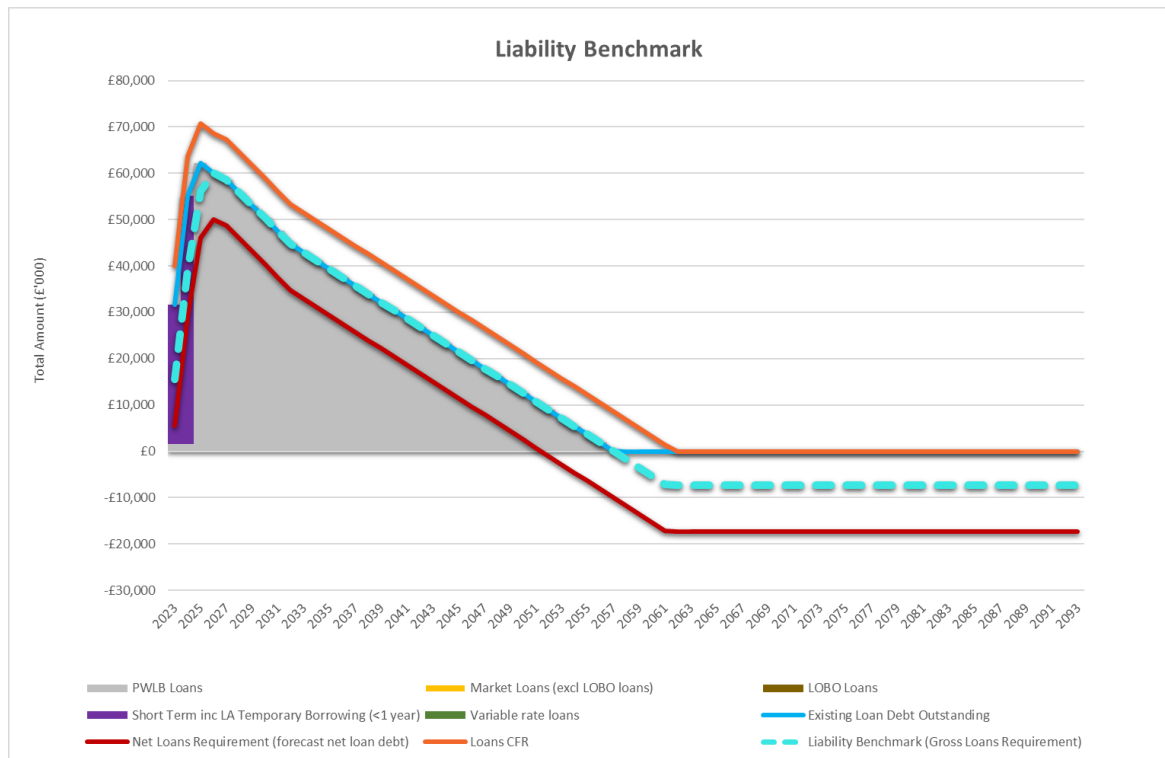
Liability Benchmark

27. To compare the Council's actual borrowing against an alternative strategy, a liability benchmark has been calculated showing the lowest risk level of borrowing. This assumes the same forecasts as table 1 above, but that cash and investment balances are kept to a minimum level of £10m at each year-end to maintain sufficient liquidity but minimise credit risk.
28. The liability benchmark is an important tool to help establish whether the Council is likely to be a long-term borrower or long-term investor in the future, and so shape its strategic focus and decision making. The liability benchmark itself represents an estimate of the cumulative amount of external borrowing the Council must hold to fund its current capital and revenue plans while keeping treasury investments at the minimum level required to manage day-to-day cash flow.

Table 2: Prudential Indicator: Liability benchmark

	31.3.23 Actual £(000)	31.3.24 Estimate £(000)	31.3.25 Forecast £(000)	31.3.26 Forecast £(000)	31.3.27 Forecast £(000)
Loans CFR	40,071	63,699	70,720	68,570	67,210
Less: Balance sheet resources	34,574	34,574	24,574	18,573	18,573
Net loans requirement	5,497	29,125	46,146	49,997	48,637
Plus: Liquidity allowance	10,000	10,000	10,000	10,000	10,000
Liability benchmark	15,497	39,125	56,146	59,997	58,637

29. Following on from the medium-term forecasts in table 2 above, the long-term liability benchmark assumes capital expenditure funded by borrowing of a maximum £62.8m, minimum revenue provision on new capital expenditure based on a 30 year asset life and income, expenditure and reserves all increasing by inflation of 2% a year. This is shown in the chart below together with the maturity profile of the council's existing borrowing:



Borrowing Strategy

30. The Authority currently holds £36.6 million of loans, an increase of £6 million on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Authority expects to borrow up to £70.7m in 2024/25. The Authority may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £140 million.
31. **Objectives:** The Authority's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving certainty of those costs over the period for which funds are required. The flexibility to renegotiate loans should the Authority's long-term plans change is a secondary objective.

32. **Strategy:** Given the significant cuts to public expenditure and in particular to local government funding, the Authority's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.
33. By doing so, the Authority is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the Authority with this 'cost of carry' and breakeven analysis. Its output may determine whether the Authority borrows additional sums at long-term fixed rates in 2024/25 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.
34. The Authority has previously raised all of its long-term borrowing from the HM Treasury PWLB Lending Facility (PWLB) (formerly the Public Works Loans Board) but will consider long-term loans from other sources including banks, pension funds and local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. PWLB loans are no longer available to local authorities planning to buy investment assets primarily for yield; the Authority intends to avoid this activity in order to retain its access to PWLB loans.
35. Alternatively, the Authority may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.
36. In addition, the Authority may borrow further short-term loans to cover unplanned cash flow shortages.
37. **Sources of borrowing:** The approved sources of long-term and short-term borrowing are:
- a. HM Treasury's PWLB Lending Facility (formerly the Public Works Loan Board)
 - b. UK Infrastructure Bank Ltd.
 - c. any institution approved for investments (see below).

- d. any other bank or building society authorised to operate in the UK.
 - e. any other UK public sector body.
 - f. UK public and private sector pension funds (except the Hertfordshire Local Government Pension Scheme).
 - g. capital market bond investors.
 - h. UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues.
38. **Other sources of debt finance:** In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:
- a. Leasing.
 - b. hire purchase.
 - c. Private Finance Initiative.
 - d. sale and leaseback.
 - e. similar asset based finance.
39. **Municipal Bonds Agency:** UK Municipal Bonds Agency plc was established in 2014 by the Local Government Association as an alternative to the PWLB. It issues bonds on the capital markets and lends the proceeds to local authorities. This is a more complicated source of finance than the PWLB for two reasons: borrowing authorities will be required to provide bond investors with a guarantee to refund their investment in the event that the agency is unable to for any reason; and there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from the Agency will therefore be the subject of a separate report to Full Council.
40. **LOBOs:** The Authority holds no LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Authority has the option to either accept the new rate or to repay the loan at no additional cost. Borrowing via LOBO loans will not be undertaken unless a separate report requesting authority is approved by Full Council.
41. **Short-term and variable rate loans:** These loans leave the Authority exposed to the risk of short-term interest rate rises and are therefore subject to the interest rate exposure limits in the treasury management indicators below. Financial derivatives may be used to manage this interest rate risk (see section below).

42. **Debt rescheduling:** The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Authority may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

Treasury Investment Strategy

43. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's treasury investment balance has ranged between £30 and £50 million, and similar levels are expected to be maintained in the forthcoming year.
44. **Objectives:** The CIPFA Code requires the Authority to invest its treasury funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Authority's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested. The Authority aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.
45. **Strategy:** As demonstrated by the liability benchmark above, the Authority expects to be a long-term borrower and new treasury investments will therefore be made primarily to manage day-to-day cash flows using short-term low risk instruments. The existing portfolio of strategic pooled funds will be maintained to diversify risk into different sectors and boost investment income.
46. The CIPFA Code does not permit local authorities to both borrow and invest long-term for cash flow management. But the Authority may make long-term investments for treasury risk management purposes, including to manage interest rate risk by investing sums borrowed in advance for the capital programme for up to three years; to manage inflation risk by investing usable reserves in instruments whose value rises with inflation; and to manage price risk by adding diversification to the strategic pooled fund portfolio. As a result we are in the process of

ending a long term investment of £10 million in the Lothbury Property Fund. The £10 million in the Hermes Property Fund will be held until the redemption restrictions on the fund are lifted in the next few years.

47. **ESG policy:** Environmental, social and governance (ESG) considerations are increasingly a factor in global investors’ decision making, but the framework for evaluating investment opportunities is still developing and therefore the Authority’s ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level. When investing in banks and funds, the Authority will prioritise banks that are signatories to the UN Principles for Responsible Banking and funds operated by managers that are signatories to the UN Principles for Responsible Investment, the Net Zero Asset Managers Alliance and/or the UK Stewardship Code.
48. **Business models:** Under the IFRS 9 standard, the accounting for certain investments depends on the Authority’s “business model” for managing them. The Authority aims to achieve value from its treasury investments by a business model of collecting the contractual cash flows and therefore, where other criteria are also met, these investments will continue to be accounted for at amortised cost.
49. **Approved counterparties:** The Authority may invest its surplus funds with any of the counterparty types in table 3 below, subject to the limits shown.

Table 3: Treasury investment counterparties and limits

Sector	Time limit	Counterparty limit	Sector limit
The UK Government	50 years	Unlimited	n/a
Local authorities & other government entities	3 years	£20m	Unlimited
Secured investments *	3 years	£20m	Unlimited
Banks (unsecured) *	13 months	£20m	Unlimited
Building societies (unsecured) *	13 months	£20m	£60m
Registered providers (unsecured) *	3 years	£5m	£30m
Money market funds *	n/a	£20m	Unlimited
Strategic pooled funds	n/a	£20m	£20m
Real estate investment trusts	n/a	n/a	n/a
Other investments *	3 years	£1m	£5m

This table must be read in conjunction with the notes below.

50. *** Minimum credit rating:** Treasury investments in the sectors marked with an asterisk will only be made with entities whose lowest published long-term credit rating is no lower than A-. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.
51. For entities without published credit ratings, investments may be made either (a) where external advice indicates the entity to be of similar credit quality; or (b) to a maximum of £500,000 per counterparty as part of a diversified pool e.g. via a peer-to-peer platform.
52. **Government:** Loans to, and bonds and bills issued or guaranteed by, national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Government are deemed to be zero credit risk due to its ability to create additional currency and therefore may be made in unlimited amounts for up to 50 years.
53. **Secured investments:** Investments secured on the borrower's assets, which limits the potential losses in the event of insolvency. The amount and quality of the security will be a key factor in the investment decision. Covered bonds and reverse repurchase agreements with banks and building societies are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the higher of the collateral credit rating and the counterparty credit rating will be used. The combined secured and unsecured investments with any one counterparty will not exceed the cash limit for secured investments.
54. **Banks and building societies (unsecured):** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.
55. **Registered providers (unsecured):** Loans to, and bonds issued or guaranteed by, registered providers of social housing or registered social landlords, formerly known as housing associations. These bodies are regulated by the Regulator of Social Housing (in England), the Scottish

Housing Regulator, the Welsh Government and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

56. **Money market funds:** Pooled funds that offer same-day or short notice liquidity and very low or no price volatility by investing in short-term money markets. They have the advantage over bank accounts of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a small fee. Although no sector limit applies to money market funds, the Authority will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.
57. **Strategic pooled funds:** Bond, equity and property funds that offer enhanced returns over the longer term but are more volatile in the short term. These allow the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Authority's investment objectives will be monitored regularly.
58. **Real estate investment trusts:** Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.
59. **Other investments:** This category covers treasury investments not listed above, for example unsecured corporate bonds and company loans. Non-bank companies cannot be bailed-in but can become insolvent placing the Authority's investment at risk.
60. **Operational bank accounts:** The Authority may incur operational exposures, for example through current accounts, collection accounts and merchant acquiring services, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments but are still subject to the risk of a bank bail-in, and balances will therefore be kept below £1 million per bank except the council's banker, Nat West, where the balance will be kept below £50 million. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than

made insolvent, increasing the chance of the Authority maintaining operational continuity.

61. **Risk assessment and credit ratings:** Credit ratings are obtained and monitored by the Authority's treasury advisers, who will notify changes in ratings as they occur. The credit rating agencies in current use are listed in the Treasury Management Practices document. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:
 - a. no new investments will be made,
 - b. any existing investments that can be recalled or sold at no cost will be, and
 - c. full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.
62. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "negative watch") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.
63. **Other information on the security of investments:** The Authority understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support, reports in the quality financial press and analysis and advice from the Authority's treasury management adviser. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may otherwise meet the above criteria.
64. **Reputational aspects:** The Authority is aware that investment with certain counterparties, while considered secure from a purely financial perspective, may leave it open to criticism, valid or otherwise, that may affect its public reputation, and this risk will therefore be taken into account when making investment decisions.
65. When deteriorating financial market conditions affect the creditworthiness of all organisations, as happened in 2008, 2020 and 2022, this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances, the Authority will

restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available to invest the Authority's cash balances, then the surplus will be deposited with the UK Government, or with other local authorities. This will cause investment returns to fall but will protect the principal sum invested.

66. **Investment limits:** The Authority's revenue reserves available to cover investment losses are forecast to be £18 million on 31st March 2024 and £18 million on 31st March 2025. In order that no more than 60% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £10 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.
67. Credit risk exposures arising from non-treasury investments, financial derivatives and balances greater than £20 in operational bank accounts count against the relevant investment limits.
68. Limits are also placed on fund managers, investments in brokers' nominee accounts and foreign countries as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

Table 4: Additional investment limits

	Cash limit
Any group of pooled funds under the same management	£20m per manager
Negotiable instruments held in a broker's nominee account	£20m per broker
Foreign countries	£5 m per country

69. **Liquidity management:** The Authority uses a spreadsheet based cash flow forecasting model to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk of the Authority being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Authority's medium-term financial plan and cash flow forecast.

70. The Authority will spread its liquid cash over at least four providers (e.g. bank accounts and money market funds) to ensure that access to cash is maintained in the event of operational difficulties at any one provider.

Treasury Management Prudential Indicators

71. The Authority measures and manages its exposures to treasury management risks using the following indicators.
72. **Security:** The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average [credit rating / credit score] of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

Credit risk indicator	Target
Portfolio average credit score	6.0

73. **Liquidity:** The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three month period, without additional borrowing.

Liquidity risk indicator	Target
Total cash available within 3 months	£10m

74. **Interest rate exposures:** This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interest rates will be:

Interest rate risk indicator	Limit
Upper limit on one-year revenue impact of a 1% <u>rise</u> in interest rates	£300,000
Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates	£300,000

75. The impact of a change in interest rates is calculated on the assumption that maturing loans and investments will be replaced at new market rates.

76. **Maturity structure of borrowing:** This indicator is set to control the Authority's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	Upper limit	Lower limit
Under 12 months	100%	0%
12 months and within 24 months	100%	0%
24 months and within 5 years	30%	0%
5 years and within 10 years	30%	0%
10 years and within 20 years	35%	0%
20 years and within 30 years	35%	0%

77. **Long-term treasury management investments:** The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The prudential limits on the long-term treasury management investments will be:

Price risk indicator	2024/25	2025/26	2026/27	No fixed date
Limit on principal invested beyond year end	£0m	£0m	£0m	£20m

78. Long-term investments with no fixed maturity date include strategic pooled funds and real estate investment trusts but exclude money market funds and bank accounts with no fixed maturity date as these are considered short-term.

Related Matters

79. The CIPFA Code requires the Authority to include the following in its treasury management strategy.
80. **Financial derivatives:** Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g. interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (i.e. those that are not embedded into a loan or investment).

81. The Authority will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.
82. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria, assessed using the appropriate credit rating for derivative exposures. An allowance for credit risk calculated using the methodology in the Treasury Management Practices document will count against the counterparty credit limit and the relevant foreign country limit.
83. In line with the CIPFA Code, the Authority will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications.
84. **Markets in Financial Instruments Directive (MFID):** The Authority has opted up to professional client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Authority's treasury management activities, the Head of Strategic Finance and Property believes this to be the most appropriate status.

Appendix A - Arlingclose Economic & Interest Rate Forecast

Underlying assumptions:

- UK inflation and wage growth remain elevated but, following a no-change MPC decision in November, Bank Rate appears to have peaked in this rate cycle. Near-term rate cuts are unlikely, although downside risks will increase as the UK economy likely slides into recession and inflation falls more quickly.
- The much-repeated message from the MPC is that monetary policy will remain tight as inflation is expected to moderate to target slowly. In the Bank's forecast, wage and services inflation, in particular, will keep CPI above the 2% target until 2026.
- The UK economy has so far been relatively resilient, but recent data indicates a further deceleration in business and household activity growth as higher interest rates start to bite. Global demand will remain soft, offering little assistance in offsetting weakening domestic demand. A recession remains a likely outcome.
- Employment demand is easing, although the tight labour market has resulted in higher nominal wage growth. Anecdotal evidence suggests slowing recruitment and pay growth, and we expect unemployment to rise further. As unemployment rises and interest rates remain high, consumer sentiment will deteriorate. Household spending will therefore be weak. Higher interest rates will also weigh on business investment and spending.
- Inflation will fall over the next 12 months. The path to the target will not be smooth, with higher energy prices and base effects interrupting the downtrend at times. The MPC's attention will remain on underlying inflation measures and wage data. We believe policy rates will remain at the peak for another 10 months, or until the MPC is comfortable the risk of further 'second-round' effects has diminished.
- Maintaining monetary policy in restrictive territory for so long, when the economy is already struggling, will require significant policy loosening in the future to boost activity.
- Global bond yields will remain volatile, particularly with the focus on US economic data and its monetary and fiscal policy. Like the BoE, the Federal Reserve and other central banks see persistently high policy rates through 2023

and 2024 as key to dampening domestic inflationary pressure. Bond markets will need to absorb significant new supply, particularly from the US government.

- There is a heightened risk of geo-political events causing substantial volatility in yields.

Forecast:

- The MPC held Bank Rate at 5.25% in November. We believe this is the peak for Bank Rate.
- The MPC will cut rates in the medium term to stimulate the UK economy but will be reluctant to do so until it is sure there will be no lingering second-round effects. We see rate cuts from Q3 2024 to a low of around 3% by early-mid 2026.
- The immediate risks around Bank Rate remain on the upside, but these diminish over the next few quarters and shift to the downside before balancing out, due to the weakening UK economy and dampening effects on inflation.
- Arlingclose expects long-term gilt yields to eventually fall from current levels (amid continued volatility) reflecting the lower medium-term path for Bank Rate. However, yields will remain relatively higher than in the past, due to quantitative tightening and significant bond supply.

	Current	Dec-23	Mar-24	Jun-24	Sep-24	Dec-24	Mar-25	Jun-25	Sep-25	Dec-25	Mar-26	Jun-26	Sep-26
Official Bank Rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.25	5.25	5.25	5.25	5.00	4.75	4.25	4.00	3.75	3.50	3.25	3.00	3.00
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
3-month money market rate													
Upside risk	0.00	0.25	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	1.00	1.00
Central Case	5.40	5.40	5.40	5.30	5.15	4.80	4.30	4.10	3.80	3.50	3.25	3.05	3.05
Downside risk	0.00	0.00	-0.25	-0.50	-0.75	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
5yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.85	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.28	4.35	4.30	4.25	4.10	4.00	3.75	3.50	3.40	3.30	3.30	3.30	3.35
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
10yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.32	4.40	4.35	4.30	4.25	4.15	4.00	3.80	3.75	3.65	3.60	3.65	3.70
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
20yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.78	4.70	4.65	4.55	4.45	4.35	4.25	4.25	4.25	4.25	4.25	4.25	4.25
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00
50yr gilt yield													
Upside risk	0.00	0.50	0.70	0.70	0.80	0.90	1.00	1.10	1.20	1.20	1.20	1.20	1.20
Central Case	4.38	4.30	4.25	4.20	4.15	4.15	4.10	4.10	4.10	4.10	4.10	4.10	4.10
Downside risk	0.00	-0.55	-0.75	-0.85	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00	-1.00

PWLB Standard Rate = Gilt yield + 1.00%

PWLB Certainty Rate = Gilt yield + 0.80%

PWLB HRA Rate = Gilt yield + 0.40%

UK Infrastructure Bank Rate = Gilt yield + 0.40%

Appendix B – Existing Investment & Debt Portfolio Position

	30/12/2023 Actual portfolio £m	30/12/2023 Average rate %
External borrowing:		
Public Works Loan Board	1.6	8.875%
Local authorities	35.0	4.020%
LOBO loans from banks		
Other loans		
Total external borrowing	36.6	4.230%
Other long-term liabilities:		
Private Finance Initiative		
Leases		
Transferred Debt		
Total other long-term liabilities		
Total gross external debt	36.6	4.230%
Treasury investments:		
The UK Government		
Local authorities		
Other government entities		
Secured investments		
Banks (unsecured)	11.3	4.800%
Building societies (unsecured)	3.0	4.880%
Registered providers (unsecured)		
Money market funds		
Strategic pooled funds		
Real estate investment trusts		
Other investments	19.9	2.723%
Total treasury investments	34.2	3.598%
Net debt	2.4	4.230%

Appendix C – Treasury Management Scheme of Delegation

Full Council

1. receiving and reviewing reports on treasury management policies, practices and activities;
2. approval of annual strategy.

Executive

1. approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices;
2. budget consideration and approval;
3. approval of the division of responsibilities;
4. receiving and reviewing regular monitoring reports and acting on recommendations;
5. approving the selection of external service providers and agreeing terms of appointment.

Audit & Governance Committee

1. reviewing the treasury management policy and procedures and making recommendations to the responsible body.
2. receiving and reviewing reports on treasury management policies, practices and activities

Appendix D – The Treasury Management Role of the Section 151 Officer

1. recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance.
2. submitting regular treasury management policy reports.
3. submitting budgets and budget variations.
4. receiving and reviewing management information reports.
5. reviewing the performance of the treasury management function.
6. ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function.
7. ensuring the adequacy of internal audit, and liaising with external audit.
8. recommending the appointment of external service providers.
9. preparation of a Capital Strategy to include capital expenditure, capital financing, non-financial investments and treasury management, with a long-term timeframe (say 20+ years – to be determined in accordance with local priorities.)
10. ensuring that the Capital Strategy is prudent, sustainable, affordable and prudent in the long term and provides value for money.
11. ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority.
12. ensure that the Authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing.
13. ensuring the proportionality of all investments so that the Authority does not undertake a level of investing which exposes the Authority to an excessive level of risk compared to its financial resources.
14. ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities.

15. provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans and financial guarantees.
16. ensuring that members are adequately informed and understand the risk exposures taken on by the Authority.
17. ensuring that the Authority has adequate expertise, either in house or externally provided, to carry out the above
18. creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following (TM Code p54): -
 - a. Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios.
 - b. Performance measurement and management (TMP2 and schedules), including methodology and criteria for assessing the performance and success of non-treasury investments.
 - c. Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making.
 - d. Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken.
 - e. Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

Agenda Item 9

East Herts Council Report

Leadership Team Meeting

Date of Meeting: Tuesday 16 January 2024

Report by: Councillor Carl Brittain – Executive Member for Financial Sustainability

Report title: Financial Management 2023/24 – Quarter 2 Forecast to Year End

Ward(s) affected: All

Summary

- The net revenue budget for 2023/24 is £12.113m as set out in table 1, this is funded by Council Tax. The forecast outturn as at 30th September 2023 predicts an overspend of £491k.
- The revised capital budget for 2023/24 is £29.552m, plus £2.954m is approved but not yet committed, as set out in Appendix C. The forecast outturn is £33.950m giving a variance of £4.398m.

RECOMMENDATIONS FOR AUDIT & GOVERNANCE COMMITTEE:

(A) The net revenue budget forecast overspend of £491k be noted;

(B) The capital programme forecast outturn of £33.950m be noted.

1.0 Proposal(s)

1.1 Not applicable

2.0 Background

2.1 The revenue budget and capital programme were approved by Council on 1st March 2023. The budgets were set amid an ongoing period of continued financial uncertainty arising from the pandemic, the lack of a multiple year Comprehensive Spending Review and risks for local government, particularly the impact of high inflation. The report provides details of the forecast outturn position against budgets set in March 2023.

2.2 The 2023/24 net revenue budget is £12.113m. the table below shows the budget alongside the 2023/24 forecast outturn as at Quarter 2. A breakdown of the revenue budget and forecast outturn can be found in **Appendix A:**

	2023/24 Budget	2023/24 Forecast outturn	Variance
	£'000	£'000	£'000
Net Cost of Services	17,230	17,873	643
Total corporate budgets	1,173	1,166	(7)
Total reserves	(818)	(963)	(145)
Total Funding	(5,472)	(5,472)	-
Net revenue spend	12,113	12,604	491
Funded by Council Tax	(12,113)	(12,113)	-
Overspend/(underspend)	-	491	491

2.3 With high inflation, the cost of living crisis has impacted on the Councils spending with contract costs, utilities and salary increases at levels above budget. Increases to the Bank of England's base rate have resulted in interest rate rises which impact on the rate at which the Council can borrow and also the return that the Council can achieve on its investments. A summary of significant variances is provided in Appendix B, this gives details of the £491k overspend.

- 2.4** The revised capital budget for 2023/24 is £29.552m, plus £2.954m approved but not yet committed, as set out in Appendix C. The forecast outturn is £33.950m giving a variance of £4.398m.

The main variances being the projected overspend on the Hertford Theatre build which officers are working to bring down and the saving achieved by the withdrawal of planned building works at Elizabeth Road. Appendix C provides a further breakdown of the capital projects.

- 2.5** The outstanding debt as at Quarter 2 was £2.5m, this is down by £1.1m from £3.6m at the end of Quarter 1 due to the payment of some large invoices. Debt over 365 days old totals £1.6m, this is being reviewed by officers. The recent restructure of the strategic finance team has resulted in an appointment to the Team Leader (transactions) post and recruitment to newly created posts in the transactions team will be completed in January 2024. The strengthening of the team, alongside the decision for credit control to be managed centrally by the finance team will improve the aged debt position of the Council.

3.0 Reason(s)

- 3.1** Section 28 of the Local Government Act 2003 requires the Council to monitor the budget and monitor and assess the adequacy of reserves and balances during the year. East Herts Council's financial management framework requires quarterly reports to Audit and Governance Committee and the Executive with expenditure forecasts to year end.
- 3.2** The Executive must consider the budget forecasts and ensure that action is taken in relation to any expenditure over spends or any underachievement of income so that the Council's

financial resources are not exceeded.

4.0 Options

4.1 Not applicable

5.0 Risks

5.1 Higher inflation and rising interest rates will put pressure on the Councils revenue and capital budgets.

6.0 Implications/Consultations

6.1 The finance team, have consulted with Heads of Service, service managers and budget managers in writing this report.

Community Safety

No

Data Protection

No

Equalities

No

Environmental Sustainability

No

Financial

All financial implications are included in the report.

Health and Safety

No

Human Resources

No

Human Rights

No

Legal

Section 28 of the Local Government Act 2003 requires the Council to monitor the budget and monitor and assess the adequacy of reserves and balances during the year. East Herts Council's financial management framework requires quarterly reports to Audit and Governance Committee and the Executive with expenditure forecasts to year end.

Specific Wards

No

7.0 Background papers, appendices and other relevant material

7.1

Appendices	
A	2023/24 Revenue budget & forecast outturn
B	Significant variances
C	2023/24 Capital programme & forecast outturn
D	Quarter two Debtors position

Contact Member Councillor Carl Brittain, Executive Member for Financial Sustainability.
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Contact Officer Steven Linnett, Head of Strategic Finance and Property, Tel: 01279 502050.
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Report Author Alison Street, Financial Planning Manager, Tel: 01279 502056. alison.street@eastherts.gov.uk

2023/24 Revenue budget - Qtr 2 Forecast outturn position

		2023/24 budget	Forecast outturn	Variance
		£'000	£'000	£'000
Net Cost of Services	Chief Executive & Directors	349	334	(15)
	Communications, Strategy & Policy	1,520	1,609	89
	HR & Organisational Development	570	578	8
	Strategic Finance & Property	2,045	2,340	295
	Corporate	546	580	34
	Housing & Health	2,193	2,187	(5)
	Democratic and Legal	1,506	1,513	7
	Planning & Building Control	2,209	2,606	397
	Operations	2,803	2,654	(149)
	Shared Revenues & Benefits Service	1,798	1,819	21
	Revenues & benefits retained costs	(467)	(507)	(40)
	Housing Benefit Subsidy	(371)	(405)	(34)
	Shared Business & Technology Services	2,291	2,327	35
	CERA	238	238	-
Total Net Cost of Services		17,230	17,873	643
Corporate Budgets	Minimum Revenue Provision	557	557	-
	Interest Payments on loans	979	1,400	421
	Interest & Investment income	(1,000)	(1,428)	(428)
	Pension Fund Deficit contribution	637	637	-
	Corporate Budgets Total:		1,173	1,166
Use of Reserves	Contributions to Earmarked reserves	590	445	(145)
	Contributions from Earmarked reserves	(1,408)	(1,408)	-
	Use of General Reserve	-	-	-
	New Homes Bonus Priority Spend	-	-	-
Net Use of Reserves:		(818)	(963)	(145)
Net Cost of Services Total:		17,585	18,076	491
Funding	Capital salaries	(150)	(150)	-
	NDR	(2,933)	(2,933)	-
	Section 31 grants	(1,169)	(1,169)	-
	(Surplus)/Deficit on collection fund	1,583	1,583	-
	Government grants	(1,361)	(1,361)	-
	Business Rates pool 22/23 pooling gain	(511)	(511)	-
	New Homes Bonus	(931)	(931)	-
Non Departmental Budgets Total:		(5,472)	(5,472)	-
Total:		12,113	12,604	491

Summary of significant variances – Qtr 2 2023/24

Budget area	2023/24 budget £000	Forecast outturn £000	Variance £000	Reason for variance
Salary budgets	15,754	15,951	197	When the 2023/24 budget was set a 4% increase on salaries was budgeted for. Following negotiations, the National Joint Council for Local Government Services has agreed a flat rate of £1,925 for all spinal points to 43 and 3.88% for all spinal points above. This has resulted in a pressure on the budget of £197k.
Planning service – staffing costs & reduced planning income	2,209	2,580	371	<p>Planning is currently forecasting to be £371k overspent at year end. At present this is due to the following:</p> <ul style="list-style-type: none"> - Decrease in planning applications as a result of rising construction costs and overall cost of living crisis. - Ongoing recruitment difficulties which has meant that the service continues to use consultants to assist with the workload and planning application backlog. <p>In terms of mitigation, planning fees are due to be increased by 35% for major applications and 25% for all other applications. Draft regulations to introduce these fee increases were laid on 20 July and need to receive parliamentary approval before coming into effect.</p> <p>A recruitment and retention strategy is in place and there is a rolling programme of recruitment. A number of posts have already been filled and it is anticipated that more will be filled in the Autumn/Winter.</p>
Restructuring costs	0	179	179	Service restructuring under the Transformation programme has resulted in costs of £179k.
Leisure contract	(150)	(258)	(108)	Income received in respect of the contract with SLM has exceeded budget by £108k as a result of a reprofiling of the income.

Budget area	2023/24 budget £000	Forecast outturn £000	Variance £000	Reason for variance
Launchpad	(16)	65	81	The set up of the Launchpad at the new space in 1 Link road was planned to take place prior to 1 st April 2023, however work did not commence until the start of April, therefore the associated costs were paid in 2023/24. Whilst furniture and other materials were reused from Charrington's House the cost of electrical works, transport, decorating, and installation exceeded the business plan estimates. Income of around £150k was budgeted for the year based on the assumption that clients would move over and be paying from 1 st April. Due to the delays in opening the space some clients had to work from home until their offices or desks were ready. In order to keep them as Launchpad members and not risk losing them, discounts were offered with the result that for April and May very little income was received. Income is forecast to be in the region of £125k for the year.
Interest payments	979	1,400	421	Due to increased bank of England base rate interest on the Councils borrowing is higher than budgeted. Officers are working hard to secure rates in advance of need that are on average 1% below the rates on deals of the day.
Investment income	(1,000)	(1,428)	(428)	Interest that the Council receives on its investments is also above budget due to the high interest rates.
Total	17,776	18,489	713	
Other minor balances	(5,663)	(5,885)	(222)	
Overall total	12,113	12,604	491	

Capital Forecast Outturn Quarter 2 September 2023

	Carry Forward from 2022/23	Revised Budget 2023/24	Forecast Outturn 2023/24	Variance 2023/24	Carry Forward to 2024/25
	£'000	£'000	£'000	£'000	£'000
Land and Buildings					
Investment in operational assets	4	254	254	0	0
Grange Paddocks Leisure Centre	97	97	97	0	0
Hartham Leisure Centre	4,300	4,496	4,496	0	0
Hertford Theatre	5,716	15,550	22,995	7,445	0
Car Park Resurfacing & extension	305	305	305	0	0
Old River Lane and Arts Centre	552	2,552	500	(2,052)	0
Northgate End	55	55	340	285	0
Elizabeth Road	1,080	1,080	0	(1,080)	0
Hostels	187	187	187	0	0
Pinehurst Community Hall	180	180	180	0	0
Vehicles and Equipment					
Rolling programme to be utilised on ICT	913	1,363	1,363	0	0
LED Lighting Upgrades	107	135	135	0	0
Community Assets					
Replacement play equipment across the district (in response to the Condition Audit to be reviewed in 2018/19)	27	77	27	(50)	0
The Wash, Hertford	50	50	50	0	0
Cannons Mill Lane, Bishops Stortford	30	30	30	0	0
Castle Park - HLF	200	2,700	2,700	0	0
Phisiobury Park - HLF	35	35	35	0	0
Buryfields	0	38	38	0	0
Revenue Expenditure Funded as Capital Under Statute (REFCUS)					
Home Improvement Loans	0	120	120	0	0
Improve & renew structures along rivers and watercourses	39	87	48	(39)	0
Land Management Asset Register & Associated Works	6	56	50	(6)	0
Green Deal Loans	0	20	0	(20)	0
Historic Building Loans	0	20	0	(20)	0
Community Capital Grants	0	65	0	(65)	0
Current Capital Programme Budget Total	13,883	29,552	33,950	4,398	0

Approved But Not Yet Committed
Buntingford Depot site works
St Andrews Street CP Resurfacing
Transformation Programme
Capital Contingency - Major Projects
Current Capital Programme Budget Total

384	repair to vehicle washer & drainage
70	
1,000	ICON & Advance
1,500	
2,954	

Capital Forecast Outturn Quarter	
	Carry Forward from 2022/23
	£'000
Land and Buildings	
Investment in operational assets	4
Grange Paddocks Leisure Centre	97
Hartham Leisure Centre	4,300
Hertford Theatre	5,716
Car Park Resurfing & extension	305
Old River Lane and Arts Centre	552
Northgate End	55
Elizabeth Road	1,080
Hostels	187
Pinehurst Community Hall	180
Vehicles and Equipment	
Rolling programme to be utilised on ICT projects subject to ITSG review	913
LED Lighting Upgrades	107
Community Assets	
Replacement play equipment across the district (in response to the Condition Audit to be reviewed in 2018/19)	27
The Wash, Hertford	50

Cannons Mill Lane, Bishops Stortford	30
Castle Park - HLF	200
Phisiobury Park - HLF	35
Buryfields	0
Revenue Expenditure Funded as Capital Under Statute (REFCUS)	
Home Improvement Loans	0
Improve & renew structures along rivers and watercourses	39
Land Management Asset Register & Associated Works	6
Green Deal Loans	0
Historic Building Loans	0
Community Capital Grants	0
Current Capital Programme Budget Total	13,883

Approved But Not Yet Committed
Buntingford Depot site works
St Andrews Street CP Resurfacing
Transformation Programme
Capital Contingency - Major Projects
Current Capital Programme Budget Total

Appendix C

2 September 2023			
Revised Budget	Forecast Outturn	Variance	Carry Forward to
2023/24	2023/24	2023/24	2024/25
£'000	£'000	£'000	£'000
254	254	0	0
97	97	0	0
4,496	4,496	0	0
15,550	22,995	7,445	0
305	305	0	0
2,552	500	(2,052)	0
55	340	285	0
1,080	0	(1,080)	0
187	187	0	0
180	180	0	0
1,363	1,363	0	0
135	135	0	0
77	27	(50)	0
50	50	0	0

30	30	0	0
2,700	2,700	0	0
35	35	0	0
38	38	0	0
120	120	0	0
87	48	(39)	0
56	50	(6)	0
20	0	(20)	0
20	0	(20)	0
65	0	(65)	0
29,552	33,950	4,398	0

384	repair to vehicle washer & drainage
70	
1,000	ICON & Advance
1,500	
2,954	

Rolling Programme

Carry forward from 2022/23 for remainder of MUGA and retention payments

The budget is still 24.105 million the expected outturn you can put as £27 million and say officer are working to bring this overspend down. The overspend is as result of inflation, supply chain shortages etc. The overspend may need to be reduced by not completing parts of the fit out, e.g. the Studio, but this will be decided by Members.

Presdales Pavillion - Porous surfacing to Car park £76k. Gascoyne Way - Concrete & Surface Repair & Lining £154k. Kibes Lane North - Refurbishment & Resurfacing £75K. Moved to approved but not yet committed.

50% of David Falco only, no other expenditure now expected for 2023/24, but we are expecting a capital receipt of £2.4m, eventually from the sales of the flats at Northgate End.

Carry forward to fund additional works required, as a result of bad value engineering. Estimated outturn due to Real are now in administration and highways works have not been completed, which will now need to be completed by another contractor.

Under spend

Hill Crest & Queens Road

SL thinks all the works here are complete but need to double check with Geoff

SL said to expect full spend as a number of major projects to be carried out this financial year

Gascoyne Way & Buntingford

Assume no spend as no programme of works has been presented apart from Folly View, Sacombe & Buryfields C/F

check ian

SL thought these were being spent, so keep as per budget at the moment

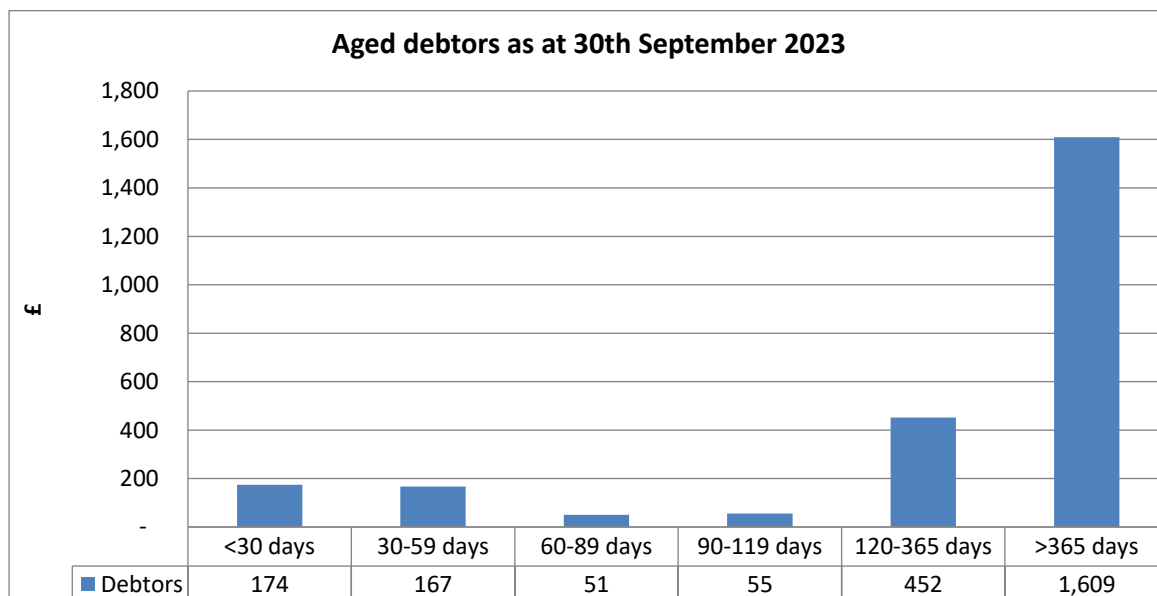
SL says there will be big expenditure here this year so need to carry forward previous years underspends to minimise overspends

No take up

No take up

Moved to revenue spend

The following graph shows the age of the £2.51m of debts outstanding as at 30th September 2023



The table below shows the aged debt by department

	As at 30/09/2023
Asset Management	344,153.98
Bed & breakfast	187,648.04
Unallocated cash	- 51,885.35
Community Safety & Health	112,472.71
Waste	2,300.09
Direct debit	50.00
Environmental Health	74,363.27
Finance	103,094.43
Grounds Maintenance	6,765.64
Housing Other	216,583.58
Launchpad	45,935.14
Legal	41,406.30
Operations Miscellaneous	559,889.48
Parking	105,927.02
Pest control	318.10
PIA	10.00
Planning	220,091.62
Hertford Theatre	3,317.99
Trade Refuse	534,671.19
Trade Waste Miscellaneous	868.58
Total	2,507,981.81

Agenda Item 14

East Herts Council Report

Audit and Governance Committee

Date of meeting: 30 January 2024

Report by: Steven Linnett, Head of Strategic Finance and Property (Section 151 Officer)

Report title: Audit and Governance Committee Work Programme

Ward(s) affected: All

Summary

- To present to Audit and Governance Committee the work programme for the year of finance and audit business with a brief summary of each report so that Members can see the business that will come before the Committee at each meeting.

RECOMMENDATIONS FOR AUDIT AND GOVERNANCE COMMITTEE

(A) Approve the work programme as set out in the report; and

(B) Specify any training requirements.

1.0 Proposal(s)

1.1 Audit and Governance Committee's audit functions are:

1.1.1 Approving the Council's statement of accounts.

- 1.1.2 Consider the effectiveness of the Council's risk management arrangements, the control environment and associated anti-fraud and anti-corruption arrangements.
- 1.1.3 Seek assurances that action is being taken on risk-related issues identified by auditors and inspectors.
- 1.1.4 Be satisfied that the Council's assurance statements, including reviewing the Annual Governance Statement against the good governance framework, properly reflect the risk environment and any actions required to improve it.
- 1.1.5 Approve internal audit's strategy, its plan and monitor its performance.
- 1.1.6 Approve the shared anti-fraud service strategy, its plan and monitor its performance.
- 1.1.7 Review summary internal audit reports and the main issues arising and seek assurance that action has been taken where necessary.
- 1.1.8 Receive the annual report of the head of internal audit.
- 1.1.9 Receive and consider the reports of external audit (including the annual audit letter) and inspection agencies, and monitor management action in response to the issues raised.
- 1.1.10 Ensure that there are effective relationships between external and internal audit, inspection agencies and other relevant bodies and that the value of the audit process is actively promoted.
- 1.1.11 Review the financial statements, external auditor's opinion and reports to Members, and monitor management action in response to the issues raised by external audit.

1.1.12 Oversight of the Council's commercial projects.

1.2 Audit and Governance Committee's finance functions are:

1.2.1 Receive budget monitoring reports and risk management reports.

1.2.2 Lead the cross-Member scrutiny and consideration of the Council's draft annual budget and medium-term financial plan.

1.2.3 Scrutinise the Council's Annual Investment Strategy, Annual Capital Strategy, Mid-Year Treasury Management Report and Annual Treasury Management Report and through review gain assurance that systems of governance and control for Treasury Management are effective.

1.2.4 Where appropriate, assisting the Council and the Executive in the development of its budget and policy framework by in-depth analysis of financial, procurement and governance related policy issues.

1.2.5 Where relevant to the audit or finance functions of the Committee, overseeing and scrutinising all Internal, Corporate and Corporate Governance functions of the Council.

1.3 In order to fulfil these functions a series of reports will be brought to Members to provide:

1.3.1 Assurance that the council's financial affairs are being properly managed and that the council is making the best use of resources;

1.3.2 An adequate and effective system of internal audit is operating and that its approved plan is being delivered;

- 1.3.3 The Council's governance arrangements are adequate;
- 1.3.4 That key business risks have been identified, evaluated and are being managed;
- 1.3.5 That key systems and controls are operating effectively giving assurance that the Statement of Accounts is materially correct and can be approved;
- 1.3.6 Receive and consider the external auditor's Audit Plan, Audit Results Report and Annual Audit Letter; and
- 1.3.7 Receive copies of Executive budget monitoring reports, for information, so that the final accounts outturn position can be compared to forecasts during the year.

2.0 Training

- 2.1 Training for Members of the Committee will be delivered for the first 30 minutes of the Committee meeting and will be related to the business before the Committee.
- 2.2 Members are recommended to review the proposed work programme and suggested training and identify any other training needs they require.

3.0 Work Programme

- 3.1 The Committee will note that the statement of accounts is shown as being approved by a sub-committee. Due to the problems in the local government external audit market, audits have been severely delayed due to the external auditor's lack of resources and therefore we cannot predict when audits will return to a firm timetable and the sub-committee is used to approve the statement of accounts as soon as practicable

after the audit is completed.

- 3.2 The work programme for the Committee is proposed to be as follows:

Committee	Date	Report Title	Report Summary
Audit & Governance Committee	May 2024	Appointment of Vice- Chairman for 2024/25	Members will vote to appoint the Vice Chairman of the Committee
		Training: Shared Anti-Fraud Service	Presentation to Members on the work of the Shared Anti-Fraud Service and the importance of tackling fraud.
		Leisure Annual Report	To present to Audit & Governance Committee an annual report on leisure so that the Committee can assure Council that the investment in new leisure centres is performing as per the business case and making a return to the council after servicing debt.
		Annual Assurance Statement and Internal Audit Annual Report	To present to Audit and Governance Committee the Annual Report on Internal Audit Activity for the preceding financial year and the level of assurance on the financial systems. Regulation 6 of The Accounts and Audit Regulations 2015 require the Council, at least once a year, to conduct a review of the effectiveness of its internal audit.
		Shared Internal Audit Service Internal Audit Plan Progress Report	To present to Audit and Governance Committee the Shared Internal Audit

Committee	Date	Report Title	Report Summary
			Service's progress against the Internal Audit Plan.
		Anti-Fraud Report	To present to Audit and Governance Committee the Shared Anti-Fraud Service's annual anti-fraud report detailing work completed on the Anti-Fraud Plan and detailing detected fraud and any recovery of monies
		Shared Anti-Fraud Service Anti-Fraud Plan Progress Report	To present to Audit and Governance Committee the Shared Anti-Fraud Service's progress against the Anti-Fraud Plan.
		Strategic Risk Register Monitoring Q4 2023/24 and Annual Review of Risk Management Strategy	To present to Audit and Governance Committee the Strategic Risk Register Monitoring at the end of quarter 4.
		Provisional Outturn 2023/24	To present to Audit and Governance Committee the provisional General Fund Revenue and Capital Outturn. The figures remain provisional until the external auditor has completed the audit
		Data Protection Update	To present to Audit and Governance Committee an update on data protection
		Audit and Governance Committee Work Programme	To present to Audit and Governance Committee an update on the work programme for the year.

Committee	Date	Report Title	Report Summary
Audit & Governance	September 2024	Training: Statement of Accounts	Presentation to Members on the key elements of the Statement of Accounts and the inter-relationship of the core statements.
		Provisional Outturn 2023/24	To present to Audit and Governance Committee the provisional General Fund Revenue and Capital Outturn. The figures remain provisional until the external auditor has completed the audit.
		Receipt of the Final External Auditor's Audit Results Report 2023/24	In accordance with the Code of Audit Practice (the Code), this report provides a summary of the work the external auditor has carried out during their audit of accounts, the conclusions they have reached and the recommendations they have made to discharge their statutory audit responsibilities to those charged with governance (in this case the Audit and Governance Committee) at the time they are considering the financial statements. In preparing their report, the Code requires them to comply with the requirements of

Committee	Date	Report Title	Report Summary
			International Standards on Auditing (United Kingdom & Ireland) – ISA (UK&I) - 260 'Communication of Audit Matters to Those Charged With Governance'.
		Approval of the Statement of Accounts 2023/24	Regulation 10 (1) of the Accounts and Audit Regulations 2015 requires the Statement of Accounts to be approved by a resolution of a committee of the Council, such approval to take place before 30 September immediately following the end of a year, or as soon as practicable after the conclusion of the audit.
		Approval of the Annual Governance Statement 2023/24	To present to Audit and Governance Committee for approval the Annual Governance Statement for incorporation in the Statement of Accounts. Regulation 6 of the Accounts and Audit Regulations 2015 requires the Council to conduct a review, at least once a year, of the effectiveness of its system of internal control and approve an annual governance statement to accompany the statement of accounts.
		Procurement Strategy 2024/5 – 2029/30 for scrutiny	To present to Audit and Governance Committee the Executive's proposed Procurement Strategy for scrutiny.

Committee	Date	Report Title	Report Summary
		Shared Internal Audit Service Internal Audit Plan Progress Report	To present to Audit and Governance Committee the Shared Internal Audit Service's progress against the Internal Audit Plan.
		Anti-Fraud Report 2023/24	To present to Audit and Governance Committee the Shared Anti-Fraud Service's annual anti-fraud report detailing work completed on the Anti-Fraud Plan and detailing detected fraud and any recovery of monies
		Shared Anti-fraud Service Anti-Fraud Plan progress report	To present to Audit and Governance Committee the Shared Anti-Fraud Service's progress against the Anti-Fraud Plan.
		Financial Management 2024/25 – Quarter 1 Forecast to Year End	To provide Audit and Governance Committee with a copy for information of the Executive Report with the forecast position on revenue spending and the capital programme as at the end of quarter 1
		Strategic Risk Register Monitoring Q1 2024/25	To present to Audit and Governance Committee the Strategic Risk Register Monitoring at the end of quarter 1.
		Data Protection Update	To present to Audit and Governance Committee an update on data protection

Committee	Date	Report Title	Report Summary
		Assets of Community Value	To present to Audit & Governance Committee the Register of Assets of Community Value annual update report.
		Audit and Governance Committee Work Programme	To present to Audit and Governance Committee an update on the work programme for the year.
Audit & Governance Committee	November 2024	Training: Treasury Management	Presentation to Members on Treasury Management and the Committee's role in overseeing treasury policies
		Annual Infrastructure Funding Statement Report 2023/24	To present to Audit and Governance Committee an update on Section 106 contributions and the council's Annual Infrastructure Funding Statement Report 2020/21
		External Audit Planning Report 2024/25	To present to Audit and Governance Committee the external auditor's Audit Planning Report. The Committee receives the report on behalf of the Council.
		Budget 2025/26 and Medium Term Financial Plan 2025/25 – 2029/30	To provide Audit and Governance Committee with an update on the budget and MTFP including costs pressures, savings and efficiencies against the original proposals, and budget planning assumptions for scrutiny.

Committee	Date	Report Title	Report Summary
		Shared Internal Audit Service Internal Audit Plan Progress Report	To present to Audit and Governance Committee the Shared Internal Audit Service's progress against the Internal Audit Plan.
		Shared Anti-fraud Service Anti-Fraud Plan progress report	To present to Audit and Governance Committee the Shared Anti-Fraud Service's progress against the Anti-Fraud Plan.
		Annual Treasury Report 2023/24	To provide Audit and Governance Committee with a copy of the Annual Treasury Report so that they can scrutinise the Report.
		Treasury Management 2024/25 Mid-Year Review	To provide Audit and Governance Committee with a copy of the Treasury Management Mid-Year Review Report so that they can scrutinise the Report
		Strategic Risk Register Monitoring Q2 2024/25	To present to Audit and Governance Committee the Strategic Risk Register Monitoring at the end of quarter 2.
		Audit and Governance Committee Work Programme	To present to Audit and Governance Committee an update on the work programme for the year.

Committee	Date	Report Title	Report Summary
Audit & Governance Committee	30 January 2024	Budget Scrutiny - Budget 2024/25 and Medium Term Financial Plan 2024-28	To present to Audit and Governance Committee the Executive's proposed General Fund Budget and Medium Term Financial Plan for scrutiny.
		Investment Strategy 2024/25 for scrutiny	To present to Audit and Governance Committee the Executive's proposed Investment Strategy for scrutiny.
		Capital Strategy and Minimum Revenue Provision Policy 2024/25 for scrutiny	To present to Audit and Governance Committee the Executive's proposed Capital Strategy and Minimum Revenue Provision Policy for scrutiny.
		Financial Management 2023/24 – Quarter 2 Forecast to Year End	To provide Audit and Governance Committee with a copy for information of the Executive Report with the forecast position on revenue spending and the capital programme as at the end of quarter 2.
		Treasury Management 2023/24 Mid-Year Review	To provide Audit and Governance Committee with a copy of the Treasury Management Mid-Year Review Report so that they can scrutinise the Report
		Shared Anti-Fraud Service Anti-Fraud Plan Progress Report	To present to Audit and Governance Committee the Shared Anti-Fraud Service's progress against the Anti-Fraud Plan.

Committee	Date	Report Title	Report Summary
		Anti-Fraud Plan	To present to Audit and Governance Committee the Shared Anti-Fraud Service Anti-Fraud Plan for the financial year.
		Shared Internal Audit Service Internal Audit Plan Progress Report	To present to Audit and Governance Committee the Shared Internal Audit Service's progress against the Internal Audit Plan.
		Internal Audit Plan	To present to Audit and Governance Committee the Shared Internal Audit Service Audit Plan for the financial year.
		Data Protection Update	To present to Audit and Governance Committee the progress on data protection policies and practices.
		External Audit Planning Report 2022/23	To present to Audit and Governance Committee the external auditor's Audit Planning Report. The Committee receives the report on behalf of the Council.
		Audit and Governance Committee Work Programme	To present to Audit and Governance Committee an update on the work programme for the year.

4.0 Reasons

4.1 To ensure that Audit and Finance Committee is aware of the work programme and ensure that Members have the opportunity to request any training or briefing around upcoming items.

5.0 Risks

5.1 Risk Management is reported to the Committee regularly.

6.0 Implications/Consultations

Community Safety

No

Data Protection

Data Protection reports and policies will be brought before the Committee as appropriate.

Equalities

No

Environmental Sustainability

No

Financial

The report details the Committee's responsibilities in relation to finance.

Health and Safety

No

Human Resources

No

Human Rights

No

Legal

Legal requirements are noted in the report summaries in the table in this report.

Specific Wards

No

7.0 Background papers, appendices and other relevant material

7.1 None

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