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Date: Wednesday, 17 January 2024

Dear Sir or Madam

The Audit Committee – Thursday, 25 January 2024, 10.30 am – Kenn Room

A meeting of the Audit Committee will take place as indicated above.

The agenda is set out overleaf.

Yours faithfully

Assistant Director Legal & Governance and Monitoring Officer

To: Members of the Audit Committee

Councillors:

Patrick Keating (Chairperson), Marcia Pepperall, Joe Tristram and Richard Tucker (Vice-Chairperson).

Independent Members: Peter Bray, Sharon Colk

This document and associated papers can be made available in a different format on request.

Agenda

1. Public Participation (Standing Order 17)

To receive written submissions from any person who wishes to address the Committee. The Chairperson will select the order of the matters to be received.

Please ensure that any submissions meet the required time limits and can be read out in five minutes (up to a maximum of 30 minutes).

Requests and full statements must be submitted in writing to the Assistant Director Governance and Monitoring Officer, or to the officer mentioned at the top of this agenda letter, by noon on the day before the meeting and the request must detail the subject matter of the address.

2. Apologies for absence and notification of substitutes

3. Declaration of Disclosable Pecuniary Interest (Standing Order 37)

A Member must declare any disclosable pecuniary interest where it relates to any matter being considered at the meeting. A declaration of a disclosable pecuniary interest should indicate the interest and the agenda item to which it relates. A Member is not permitted to participate in this agenda item by law and should immediately leave the meeting before the start of any debate.

If the Member leaves the meeting in respect of a declaration, he or she should ensure that the Chairperson is aware of this before he or she leaves to enable their exit from the meeting to be recorded in the minutes in accordance with Standing Order 37.

4. Minutes of the meeting held on 23 November 2023 (Pages 5 - 10)

23 November 2023 to approve as a correct record (attached)

5. Matters referred by Council, the Executive, other Committees and Panels (if any)

None

6. Council Spending Controls (Pages 11 - 16)

Report of the Director of Corporate Services (attached)

7. Audit Committee Workplan (Pages 17 - 18)

Audit Committee Workplan of the Chairperson of Audit Committee and Director of Corporate Services (attached)

8. Annual Governance Statement 2023/24 (Pages 19 - 24)

Report of Head of Audit and Assurance (attached)

9. **Internal Audit Plan 2024/25** (Pages 25 - 28)

Report of Head of Audit and Assurance (attached)

10. **North Somerset Council - Audit Progress Report and Sector Update** (Pages 29 - 62)

Report of External Auditors (attached)

11. **Treasury Management Strategy 2024/25** (Pages 63 - 106)

Report of Head of Finance (attached)

12. **Update of the Annual Accounts and Accounting Policies** (Pages 107 - 118)

Report of Head of Finance (attached)

13. **Urgent business permitted by the Local Government Act 1972 (if any)**

Any item of business which the Chairperson is of the opinion should be considered at the meeting as a matter of urgency by reason of special circumstances (to be specified in the Minutes). For a matter to be considered as an urgent item, the following question must be addressed:

“What harm to the public interest would flow from leaving it until the next meeting?” If harm can be demonstrated, then it is open to the Chairperson to rule that it be considered as urgent. Otherwise the matter cannot be considered urgent within the statutory provisions.

Exempt Items

Should the Audit Committee wish to consider a matter as an Exempt Item, the following resolution should be passed -

“(1) That the press, public, and officers not required by the Members, the Chief Executive or the Director, to remain during the exempt session, be excluded from the meeting during consideration of the following item of business on the ground that its consideration will involve the disclosure of exempt information as defined in Section 100I of the Local Government Act 1972.”

Also, if appropriate, the following resolution should be passed –

“(2) That members of the Council who are not members of the Audit Committee be invited to remain.”

Mobile phones and other mobile devices

All persons attending the meeting are requested to ensure that these devices are switched to silent mode. The chairman may approve an exception to this request in special circumstances.

Filming and recording of meetings

The proceedings of this meeting may be recorded for broadcasting purposes.

Anyone wishing to film part or all of the proceedings may do so unless the press and public are excluded for that part of the meeting or there is good reason not to do so, as directed by the Chairperson. Any filming must be done as unobtrusively as possible from a single fixed position without the use of any additional lighting, focusing only on those actively participating in the meeting and having regard to the wishes of any members of the public present who may not wish to be filmed. As a matter of courtesy, anyone wishing to film proceedings is asked to advise the Chairperson or the Assistant Director Legal & Governance and Monitoring Officer's representative before the start of the meeting so that all those present may be made aware that it is happening.

Members of the public may also use Facebook and Twitter or other forms of social media to report on proceedings at this meeting.

Emergency Evacuation Procedure

On hearing the alarm – (a continuous two tone siren)

Leave the room by the nearest exit door. Ensure that windows are closed.

Last person out to close the door.

Do not stop to collect personal belongings.

Do not use the lifts.

Follow the green and white exit signs and make your way to the assembly point.

Do not re-enter the building until authorised to do so by the Fire Authority.

Go to Assembly Point C – Outside the offices formerly occupied by Stephen & Co

North Somerset Council

Minutes

of the Meeting of

The Audit Committee
Thursday, 23 November 2023

Kenn Room

Meeting Commenced: 10.30 am Meeting Concluded: 12.01 pm

Councillors:

Patrick Keating (Chairperson)
Richard Tucker (Vice-Chairperson)
Marcia Pepperall

Absent: Councillors: Joe Tristram.

Also in attendance: Barrie Morris, Grace Hawkins (Grant Thornton)

Officers in attendance: Amy Webb (Director of Corporate Services), Melanie Watts (Head of Finance), Mark Anderson (Principal Accountant (Resources), Peter Cann (Head of Audit and Assurance), Alex Stafford (Emergency and Business Continuity Manager) and Philippa Penney (Head of Democratic and Electoral Services).

AUD 10 Public Participation (Standing Order 17)

None.

AUD 11 Declaration of Disclosable Pecuniary Interest (Standing Order 37)

None declared.

AUD 12 Minutes 21 September 2023

Resolved: that the minutes of the meeting be approved as a correct record

AUD 13 Matters referred by Council, the Executive, other Committees and Panels (if any)

None.

AUD 14 Q2 Risk Management update 2023-24

The Director of Corporate Services presented the report.

Members were familiar with the risk register and how it fed into the corporate risk registers. There were some additions of new principal risks and a new strategic risk surrounding artificial intelligence (AI). Ongoing financial pressures remained the most significant risk. Issues were being grouped into headline themes, such as finance and capital value.

Whilst there were no specific issues regarding the impact of Reinforced Autoclaved Aerated Concrete (RAAC) on our buildings, maintenance of council owned estate remained a risk.

The ICT Infrastructure Board had approved an AI policy which addressed how it should be used across the organisation. Encouragement was to use AI, but that any such use must be per the policy. Agilisys was supporting an exploration of potential systems that could be used, with the emerging themes being used to form a business case. Any decision-making software must not be discriminatory and, whilst human decision making was not free from error, the expectation placed on AI was that of high accuracy.

Coastal flooding posed a principal risk for North Somerset, more so than surface water flooding caused by extreme weather. The concern from residents had been exacerbated by the maps published by the Environment Agency so far showing only the unmitigated risks, but this was being addressed to take the mitigation impacts into account.

Members discussed any underlying risk for North Somerset arising from the financial position of Somerset Council. The Director confirmed that our own financial position had been addressed in the MTFP report being considered by the Executive next week. Implications for services delivered by Somerset Council were being monitored but there were no risks of failure at present. The underlying risk management remained robust, and the Somerset experience seemed to stem from the amassed district budget shortfalls rather than failures to governance and decision making. Grant Thornton was due to publish a national report on failing councils on 8 December and would include this on the committee agenda for January.

Shared service arrangements with Somerset Council did still exist e.g., Registrars, but the majority were brought back in house over the last year or so. It was also confirmed that, whilst there was legal provision for a local authority to lend money to another, North Somerset had not lent any money to Somerset. Members discussed potential future impacts to public transport and bus routes resulting from changes being made in Somerset and agreed to keep it in view.

Barrie Morris took the opportunity to introduce Grace Hawkins who would be replacing him following the 5 yearly auditor rotation. Grace would be presenting the annual report to committee in January.

Resolved: that the Audit Committee noted the Q2 updates to the 2023/24 strategic risk register and escalated risks from the directorate risk registers

AUD 15 **Internal Audit Update Report November 2023**

The Head of Audit & Assurance presented the report which covered both internal audit and fraud from 1st April to 1st November 2023.

No significant issues had been reported this year. Highlighted points were in relation to whistleblowing and were broadly related to a theme of non-compliance in following the leave recording policy. Whilst this had proved to be a unique example rather than a regular occurrence, HR were reviewing the policy to strengthen for the future. Use of the whistleblowing process underlined confidence in the referral process.

Unplanned work had taken place regarding the Clevedon seafront, with a lessons learned review that considered decision making, engagement, and project management arrangements for this specific project. This was separate to the AECOM review who were looking at how the scheme in place was working in practice so a different perspective from audit.

The Director of Corporate Services gave assurance that the Banwell bypass had been managed very differently and did not encounter the same issues as experienced at Clevedon. Whilst there were unavoidable risks associated with Banwell, it was a much bigger scheme and therefore subject to greater scrutiny and governance.

National advice and guidance had been shared during fraud awareness week and the Chief Executive had reiterated the messaging in her weekly email to all staff.

The table on page 26 of the report detailed the data analytics work detecting fraud and error within the council. Whilst nearly all duplicate payment had been identified and resolved, further work was underway to minimise occurrences in the first place. It was confirmed that, whilst the administrative cost of recovery was minimal, North Somerset would be benchmarked against other authorities for reassurance.

The National Fraud Initiative considered data sets externally, and discussion included estimated savings from blue badges and notification of deaths by using Tell Us Once. This would be included in the internal audit plan for next year.

The committee were given an update on progress against planned internal audit work throughout the year. Three had been deferred due to the time taken on unplanned work such as Clevedon. The deferred items were lower risk and had been agreed with the directorate (Place).

The majority of recommendations were yet to be implemented but were being kept in view to ensure progress. None were overdue. An update would be provided to the next meeting.

Resolved: that the Audit Committee:
- Noted the progress in delivery of the 2023/24 Annual Internal Audit Assurance Plan; and
- Noted the associated Fraud prevention and unplanned work that had been completed

AUD 16 **2023/24 Treasury Management Mid-year Report and 2024/25 Strategy Update**

The Principal Accountant (Resources & Financial Planning) presented this mid-year report containing a six-monthly update against the strategy that had been set in February.

It was suggested that interest rates were at or near their peak and that the inflation rate was improving. It was confirmed that the £5.97m estimate for investment income was realistic. Returns of 4.6% were broadly in line with expectations. Borrowing requirement levels had been reprofiled with no additional funding being drawn down at 30th September.

Non-treasury management activity actively comprised commercial investments with a forecast annual yield of 0% which shows the council is not overly reliant on commercial activity to support the revenue budget. The Sovereign Centre continues to offer retail and non-retail activity and the council recognised the longer-term place-shaping impacts these assets had on the local area.

The CIPFA code of practice set out the indicators required to report against, all of which had been complied with. The 2023/24 strategy also contained approved counterparty limits which, other than one non-material exception, were also complied with.

The balance sheet summary reflected a higher investment level than expected, but this was due to two large lump sum annual funding amounts from WECA and the Integrated Care Board received in September.

The investment strategy for next year would be brought to committee in January. Whilst no major changes were anticipated, the report would seek to formalise the Environmental, Social, Governance (ESG) policy framework within that strategy.

The table of limits aimed to avoid over exposure to a single counterparty.

The public works loan board was a complex organisation albeit relatively easy to access funds from. It couldn’t be used to fund commercial or revenue expenditure, and all borrowing facility would be cut off if used outside the regulations. Spending returns were submitted to government and had to detail exactly what we spent it on, matching the original criteria.

Resolved: that the Audit Committee noted
- the in-year treasury management performance to 30 September 2023 which included performance, prudential indicators, and commercial investments; and
- the proposed matters for inclusion in the treasury management strategy 2024/25

AUD 17 **Business Continuity Co-Ordination - Update Report**

The Emergency and Business Continuity Manager presented the report. The requirement to have a Business Continuity management strategy was built in to the Civil Contingencies Act and imposed a statutory duty on all category 1 responders to have business continuity plans in place.

A template plan had been developed for the critical services which had been identified by each of the directorates. These included instructions as to procedures that would need to be implemented including impact analysis and contingency work around key issues such as IT provision and staff. Business impact analysis didn't look at specific risks but rather covered a multitude of different scenarios. It had been rolled out across 88% of critical services, and current work was with children's services, bringing in the other 12% by 5th December. Plan maintenance would be ongoing thereafter.

One of the key requirements was for training and exercising. Workshops had been held with critical services throughout the last 2 years to help inform the plans. A test had been conducted for a strategic level IT outage, and the actions from that exercise were 86% complete. The test was to be rerun on 20th March 2024. The intention is to then consider business continuity testing more at directorate and service level.

The Business Continuity team were working with the accommodation strategy programme team to support the move out of Castlewood. The current arrangement of 2 separate buildings provided some redundancy e.g., in power generation at Castlewood. Castlewood also currently housed the emergency control centre, so consideration was being given as to an appropriate equivalent in the Town Hall.

The community resilience event in May 2023 worked with the voluntary sector. It was hosted by Voluntary Action North Somerset (VANS) and focussed on the impact of climate change. The Emergency and Business Continuity Manager gave a 2 hour presentation on the risks of climate change and the risks of severe weather impacts on volunteers and service users.

There was a significant resource issue for the team, being a small team of 1.5 fte staff plus the manager. Two areas of planned work had not yet been completed i.e. updating the corporate strategy and the corporate plan, but these were being prioritised for next year.

Ongoing operational work included reviewing the contractors and suppliers for their own business continuity arrangements. There was also the maintenance and cyclical review of plans, exercises, and response to regional events.

There were no direct climate change and environmental impacts to the team as these rested with each of the services to consider in their own planning, but severe weather events impacted on business continuity in general.

The National Security risk assessment was produced at a national level and looked at UK wide risks. Whilst it was not public facing, a public version was available in summary although it still remained a large document. It was localised to the community risk register which covered the whole of the Avon & Somerset police area. This was also fed into the Principal Risks as presented in the Strategic Risk Register presented elsewhere on the agenda.

The biggest threat both on emergency management and business continuity was that of coastal flooding. Three of the main settlements in North Somerset were on the coast and all three would be impacted, including the Town Hall. Hybrid working had addressed some of the risks, as the organisation had become adept at working at various locations, not just in the office or at home. This had also created additional risks as staff were spread more widely. Regional or wide-spread power cuts were a risk to back-up power generation, particularly for those working at home.

Hinkley Point was identified as a significant risk, and the team were working with Somerset Council who led on contingency arrangements. There was a requirement to plan for emergencies at all radiological sites.

The team focused much of their time on risk management and provided a 24/7 response rota with specialist knowledge and dispersal dissemination arrangements.

Liaison with the fire authority was through the statutory Local Resilience Forum (LRF) which mirrored each of the police force areas. It entailed multi-agency engagement including the fire authority and other emergency responders. The LRF reviewed and assessed risks, drawing up and implementing plans.

It was agreed that the role of elected members in the event of a critical incident should be included in a short guidance document or training/briefing session. It was agreed that this should be included in the suite of information provided for member induction.

Resolved: that the Audit Committee noted the update on Business Continuity co-ordination.

AUD 18 **Urgent business permitted by the Local Government Act 1972 (if any)**

None.

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Chairperson

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North Somerset Council

Report to the Audit Committee

Date of Meeting: 25 January 2024

Subject of Report: Revenue Budget update for 2023/24

Town or Parish: All

Officer/Member Presenting: Amy Webb, Director of Corporate Services

Key Decision: N/A
Reason: Not an Executive decision

Recommendations

To note the increasing pressures on the council's revenue budget and support the emergency measures that are being put into place by the Corporate Leadership Team to control spending.

1. Summary of Report

The purpose of this report is to share an update on the council's financial position and to advise of the emergency measures that are being implemented to enable the council to control spending as part of its plans to end the financial year without an overspend.

2. Policy

The council's budget monitoring is an integral feature of its overall financial and assurance framework, ensuring that resources are planned, aligned and managed effectively to achieve successful delivery of its aims and objectives.

The increasing demand for some of our key statutory services as well as the broader economic position mean that the council is exposed to a rapidly changing environment. Understanding the financial consequences and reporting issues through our monitoring framework is increasingly crucial.

3. Details

The latest budget monitoring report was considered by the Executive at their meeting on 6 December 2023 and at that time the council was forecasting an overspend of £672,000. It should be noted that this is a net position and combines several areas where services are under extreme pressure and projecting to overspend their budgets, as well as other areas which have identified savings or increased income to help mitigate some of the pressures.

The forecasts within the report were based on information collected at the end of September and have since been updated. The latest assessment shows that the cost pressures are continuing to increase and that the projected overspend for all council services has **increased to £2.3m** for the year.

Like many other councils, North Somerset is facing increasing demand for our services, notably in areas such as social care and transporting children so that they can attend school, as well as inflation, which has increased the cost of our external contracts. The income we receive to fund these costs is fixed and does not increase which means that the council is left with knowing that it has a budget gap and also a legal requirement to balance the budget at the end of each financial year.

Whilst the council has a good track record of delivering budget savings and balancing its budget over recent years, our monitoring shows that our unfunded pressures are now restricting our ability to balance the budget for the year without taking some action which looks to focus resources on delivering essential council services.

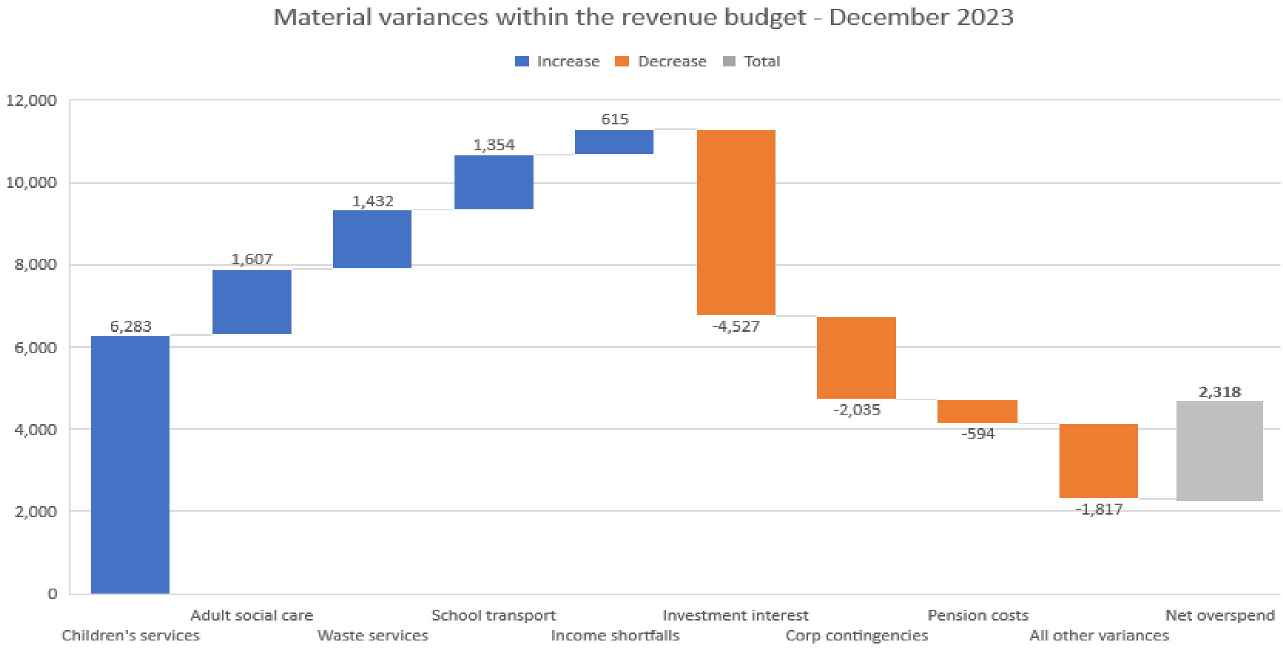
We have already implemented a number of measures to help us to reduce the overspend and colleagues across the organisation have worked collectively and collaboratively to do all they can, but due to the increasing costs of care, especially for vulnerable children, further changes are needed to close the budget gap and given that we only have three months to do this, we plan to implement measures immediately.

We do recognise that some of the planned measures will impact on the delivery of services to residents and the wider community although efforts will be made to protect and prioritise statutory services that benefit those most in need. We will also look to ensure that we let communities know of any impacts that will affect them.

These measures are necessary and will not only help us to close the budget gap for the current financial year but given that we still face a challenging financial situation for next year and beyond, the measures will also provide a focus to be able to balance the draft budget for 2024/25 and hopefully enable the council to avoid some of the longer-term financial difficulties that other councils have experienced.

Material budget pressures and mitigations included within the latest forecast are shown in the table and graphic below.

Issue	£000
Material budget pressures within services	
Children's services – placement costs, including disabled children's packages and community support	6,283
Home to School Transport costs	1,354
Adults – care in the community support costs	1,432
Waste services	1,432
Corporate contract costs and income short-falls	615
Sub total	**11,291**
All other budget variances and mitigations	
Release of the council's corporate contingencies and provisions	(2,035)
Net increase in interest received on investments	(4,527)
Reduction in the council's past service pension contribution	(594)
Other budget variances within directorates	(1,817)
Sub total	**(8,973)**
Forecast overspend at Month 8	**2,318**



A summary of the emergency budget actions that will be implemented are;

- Revised vacancy management process which will require the corporate leadership team to approve all recruitment decisions for new and existing vacant posts and changes to contracts; this will mean that only posts that deliver essential or statutory services will be filled. A new process and template have been created and will be cascaded to all managers to understand the specific impact of each request.

- Spending controls which will require directors, assistant directors and heads of service to approve spending before a financial commitment is made; this will ensure that only essential spending that supports the delivery of statutory services will be incurred and non-essential spending is deferred. A retrospective review of all transactions will be carried out to ensure compliance with the new arrangements.

- Review and reprioritisation of ear-marked reserves by directors; this will mean that non-essential spending is stopped so that the resources can be released and used to support current budget pressures.

The council's financial arrangements are complex and there are many contractual and legal obligations to consider which means that there are likely to be some exceptions to the principles listed above however, the council is confident that should these measures be implemented and followed, then we should be able to achieve a balanced budget by the end of the year and provide a stable platform for the beginning of next year. It is anticipated that these measures will remain in place for at least six months and until we can determine that our financial position has stabilised with spending forecasts once again within approved limits.

4. Consultation

Internal consultation has been undertaken as part of the ongoing financial monitoring processes and includes senior officers and executive members.

5. Financial Implications

Financial implications have been included within the body of the report.

6. Legal Powers and Implications

The Local Government Act 1972 lays down the fundamental principle by providing that every local authority shall make arrangements for the proper administration of their financial affairs including balancing their budgets each year from within their own resource allocations.

Further requirements are contained within the Local Government Act 1988, Section 114 (3) which provide for instances whereby the chief finance officer of an authority makes a judgement that the expenditure of the authority in a financial year is likely to exceed the resources available.

7. Climate Change and Environmental Implications

There are no specific climate change or environmental implications to note within this report.

8. Risk Management

The council's Strategic Risk Register includes a specific risk associated with managing the council's in-year spending.

Risk	Inherent risk score	Residual Likelihood	Residual Impact	Residual Risk Score	Comments
Risk that we do not manage budgets effectively in-year, including by not implementing and delivering the savings or transformational projects required to meet the financial challenge	HIGH	5	4	HIGH	This reflects the council-wide position which incorporates many risks with a potential financial impact at the highest level within the matrix

The council's corporate leadership team routinely review the budget monitoring forecasts as well as significant risks which may emerge from within directorate risk registers or operational activities, which may also have a financial consequence and take appropriate action as needed. This report is an escalation of that process.

The latest budget forecasts do assume a cost projection to the end of the financial year based on assumed levels of cost and demand, there remains an inherent risk that both costs and demand for services continue to grow, which would further increase the overspend and the need for further mitigation.

9. Equality Implications

There are no specific equality implications with regard to the recommendations contained within this report although it should be noted that the council's spending controls will maintain the delivery of statutory services, which often support vulnerable residents or those most in need.

10. Corporate Implications

The council's performance framework and financial monitoring processes are vital tools in ensuring that services are focused on delivery of statutory services and agreed priorities and that with continuing financial pressures and demands for services, resources are re-prioritised and allocated to those areas in the first instance.

11. Options Considered

None – the council is legally required to set a balanced budget and to implement a robust financial framework to ensure that spending is aligned to available resources and all available options to achieve this are considered within the details above.

Author:
Melanie Watts, Head of Finance, melanie.watts@n-somerset.gov.uk
Amy Webb, Director of Corporate Services, amy.webb@n-somerset.gov.uk

Appendices:
None

Background Papers:
Exec reports:

- Medium Term Financial Plan and Revenue Budget for 2023/24, February 2023
- MTFP and Revenue Budget updates and also Budget Monitoring Reports 2023/24, September, October and December 2023
-

Council report: February 2023, Council Tax Setting 2023/24

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Audit Committee Formal Meetings Work Plan - which set out provisional agendas for forthcoming meetings							
Title	**Frequency**	**Lead Officer**	**Purpose of Report**	**Jan-24**	**Apr-24**	**Sep-24**	**Nov-24**
Annual Letter of Representation	Annual	Committee chair/ Dir Corporate Services	Letter of Representation reagding External audit				
Audit Committee Workplan	Annual	Committee chair/ Dir Corporate Services	Member Information and Assurance				
Report of Work Undertaken by Audit Committee	Annual	Committee Chair/ Head of Internal Audit	Member Information and Assurance				
Annual Governance Statement Approach	Annual	Head of Internal Audit	Member Information and Engagement on the approach to developing the AGS				
Annual Governance Statement (Draft)	Annual	Director of Corporate Services	To present the draft AGS for consideration of matters of risk, governance, internal control				
Annual Governance Statement (Final)	Annual	Director of Corporate Services	To present the AGS for consideration of matters of risk, governance, internal control, and associated Annual Governance Statement Action Plan				
Business Continuity Governance	Annual	Emergency Manager	Risk Management Governance				
Annual Audit Letter (EA)	Annual	External Auditors	To provide those charged with Governance the External Audit Findings on the Quality of the Statement of Accounts and Annual Governance Statement, to provide Independent Assurance				
External Auditor (EA), audit plan	Annual	External auditors	To provide those charged with Governance the forward plan for External audit engagement				
Annual Auditors report	Annual	External Auditors/ Dir Corporate Services	To provide those charged with Governance the External Audit Findings on value for money at the council				
External Audit (EA) Findings Report/Audit Opinion	Annual	External Auditors/Head of Finance	To provide those charged with Governance the External Audit Findings on the Quality of the Statement of Accounts and Annual Governance Statement, to provide Independent Assurance				
Risk Management Framework Update	Annual	Head of Business Insight, Policy and Partnerships	Risk Management Governance				
Annual Statutory Accounts (Draft)	Annual	Head of Finance	Draft Statement of Accounts				
Annual Statutory Accounts (Audited)	Annual	Head of Finance	Audited Statement of Accounts				
Accounting Policies	Annual	Head of Finance	Finance Governance and Assurance				
Treasury Management 2023/24 Quarter 2 /mid-year and 2024/25 Draft TM Strategy update	Annual	Head of Finance	Treasury Management Quarterly update and look ahead at next year's Treasury management Strategy				
Treasury Management Strategy 2024/25	Annual	Head of Finance	Treasury Management Strategy Governance Assurance				
Treasury Management 2024/25 Quarter 3 performance	Annual	Head of Finance	Treasury Management Quarterly update				
Treasury Management 2023/24 Quarter 4 performance /outturn and 2024/25 Quarter 1 performance	Annual	Head of Finance	Annual Treasury Management Outturn and Quarterly update				
Treasury Management 2024/25 Quarter 2 /mid-year and 2025/26 Draft TM Strategy update	Annual	Head of Finance	Treasury Management Quarterly update and look ahead at next year's Treasury management Strategy				
Counter Fraud - Annual Anti-Bribery, Fraud and Corruption Policy/Report	Annual	Head of Internal Audit	Annual Report on progress/ activity				
Internal Audit Plan - Draft	Annual	Head of Internal Audit	Consultation and proces paper				
Internal Audit Plan	Annual	Head of Internal Audit	IA Plan for Ctte sign-off				
Review of Minutes and Matters Arising from previous meetings	Quarterly	Committee chair/ Dir Corporate Services	Review of actions and matters brought forward from previous meetings				
Risk Register updates - NSC	Quarterly	Head of Business Insight, Policy and Partnerships	Corporate Governance monitoring				
Internal Audit (IA) updates and Annual Report	Quarterly	Head of Internal Audit	Internal Audit Assurance				
External Auditor (EA), progress update	Six monthly	External Auditors	To provide those charged with Governance the External Audit Findings on the Quality of the Statement of Accounts and Annual Governance Statement, to provide Independent Assurance				
Treasury Management (TM) performance/ outturn	Six monthly	Head of Finance	Annual Treasury Management Outturn				

Title	**Frequency**	**Lead Officer**	**Purpose of Report**	**Jan-24**	**Apr-24**	**Sep-24**	**Nov-24**
Governance - ad hoc reports when changes happen, a risk arises which requires additional assurance or as a result of audit recommendations							
ICT Security update	When required	Head of ICT					
Updates to the Constitution and Financial Reg	When required	Monitoring Officer	To review and approve changes to the Councils constitution ahead of the annual general meeting				

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Agenda Item 7

North Somerset Council

Report to the Audit Committee

Date of Meeting: 25th January 2024

Subject of Report: Annual Governance Statement 2023/24

Town or Parish: None

Officer/ Member Presenting: Peter Cann - Audit West

Key Decision: No

Recommendations

The Audit Committee notes the report and process for the Annual Governance Statement.

1. Summary of Report

This report provides a brief overview of the process for completion of the Annual Governance Statement for 2023/24.

Whilst the statement is prepared and authorised by management and the Leader of Council, the Audit Committee has specific terms of reference given to it which requires it to consider the Annual Governance Statement and the framework which supports it which includes primarily the local code of corporate governance.

The Committee are asked to note that whilst this report describes the outline process for completion of the statement, work will be completed with the Councils Section 151 Officer as the statement is compiled to identify any detailed parts of the process which may benefit from being refreshed. Ahead of this, any comments from the Committee regarding are welcomed.

Members are advised that feedback previously provided by the Audit Committee in respect of amendments to wording and presentation was accepted and contained within the 2022/23 statement.

2. Policy

2.1 The council has adopted a Local Code of Corporate Governance, which is consistent with the principles of the CIPFA/SOLACE Framework *Delivering Good Governance in Local Government*.

2.2 The Annual Governance Statement explains how North Somerset Council has complied with the Local Code of Corporate Governance and also meets the requirements of:

- The Accounts and Audit (England) Regulations 2015, specifically Regulation 4 (2) in respect of the annual review of the effectiveness of its system of internal control and Regulation 4 (4) in respect of the preparation and publication of an Annual Governance Statement.

3. Details

3.1 **Background –**

The Annual Governance Statement is based on a 'Local Code of Corporate Governance' which forms part of the Council's Constitution. As the Annual Governance Statement is statutory we are required to take account of any guidance which is provided by CIPFA/SOLACE.

This guidance is also used by the External Auditor in their audit of the accounts and we are therefore required to take account of these in preparation of the statement.

Delivering Good Governance in Local Government; Framework, published by CIPFA in association with SOLACE, sets the standard for local authority governance in the UK. The concept underpinning the framework is to support local government in taking responsibility for developing and shaping an informed approach to governance, aimed at achieving the highest standards in a measured and proportionate way.

The purpose of the Framework is to assist authorities individually in reviewing and accounting for their own unique approach, with the overall aim to ensure that:

- Resources are directed in accordance with agreed policy and according to priorities
- There is sound and inclusive decision making
- There is clear accountability for the use of those resources in order to achieve desired outcomes for service users and communities

Governance is a term used to describe the arrangements (including political, economic, social, environmental, administrative, legal, and other arrangements) put in place to ensure that the intended outcomes for stakeholders are defined and achieved.

Good governance enables the Council to effectively achieve its intended outcomes, whilst acting in the public interest at all times.

Our code is based on the following key principles of good governance –

- Behaving with integrity, demonstrating strong commitment to ethical values and respecting the rule of law
- Ensuring openness and comprehensive stakeholder engagement
- Defining outcomes in terms of sustainable, economic, social and environmental benefits
- Determining the interventions necessary to optimise the achievement of the intended outcomes
- Developing the entity's capacity, including the capability of its leadership and the individuals within it
- Managing risks and performance through robust internal control and strong public financial management
- Implementing good practices in transparency, reporting and audit, to deliver accountability

The Code provides further detail for each of the key principles to describe expectations and is used as part of the Annual Governance Review each year. Last year's Annual Governance Statement can be seen in the link here.

3.2 Process for 2023/24 Statement

An overview of the general process for the compilation and approval of the Annual Governance Statement for 2023/24 is attached at the end of this report at Annex A. This is similar to the process adopted in previous years but will be reviewed during each stage of completion alongside the Council's Section 151 Officer to identify any ways in which the process could be further enhanced.

The process diagram indicates the major steps in the process for compiling the statement and the outcome will be a final Annual Governance Statement ratified by the Audit Committee as part of the Annual Accounts approval process.

CIPFA/SOLACE guidance as detailed above and its key principles will be taken account of as normal within this year's review and as reported last year, there were three significant issues identified in the 2022/23 statement; i) the financial challenge, ii) Ofsted/ Children's Services and iii) Rising Dedicated School's Grant (DSG) deficit.

The definition of a significant issue can be summarised as one of the following –

- Significant failures in decision making at Council or Executive
- Significant unexpected use of Resources
- Significant performance failings or failures in service delivery
- Significant issues from inspections, audits, complaints etc
- Significant issues failures in respect of statutory duties
- Significant issues from operational issues and third parties

Whilst the statement forms part of the Annual Accounts it is a separate document and is a management statement which is signed/ authorised by the Chief Executive and Leader of Council before being presented to the Audit Committee.

4. Consultation

This report describes the Annual Governance Review process which members are invited to comment upon. As part of wider and ongoing consultation, the 2023-24 Annual Governance Statement will also be updated to reflect any feedback provided by Committee Members.

5. Financial implications

The Annual Governance Statement describes how the council complies with its Local Code of Governance which incorporates all the council's business and hence budget.

6. Legal Powers and Implications

Accounts & Audit Regulations set out the expectations of provision of an Annual Governance Statement. This is supported by CIPFA/SOLACE standards and the Council's Local Code of Corporate Governance. Implications of not providing this statement would include potential qualification of the Accounts, increase in External Audit fees, potential significant reputational risks and ultimately additional costs to rectify.

7. Climate Change & Environmental Implications

No direct implications however the review process will consider key risks (& assurances) which may include Climate Change and any significant issues where appropriate.

8. Risk Management

Failure to compile an Annual Governance Statement would result in non-compliance with statutory legislation and leave the Council open to criticism by External Audit and external stakeholders.

9. Equality Implications

None.

10. Corporate Implications

The production of an Annual Governance Statement is an explicit statutory requirement of the Accounts and Audit (England) Regulations.

The completed Annual Governance Statement is reviewed by the Council's External Auditor.

11. Options Considered

None, this is a statutory process.

AUTHOR

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BACKGROUND PAPERS

Council's Local Code of Corporate Governance

Annex A. Outline Methodology for Preparing the Annual Governance Statement 2023/24

Independent Assurance

- Audit Plan & Outcomes of work
- Head of Audit opinion
- Annual Audit Plan
- Counter fraud activity and investigations
- Risk Management

Senior Management

- Corporate Leadership Team
- Finance Business Partners
- Medium term financial plans and savings programmes
- Partnership working
- Client/Contract Management

Performance management

- Corporate Plan
- Performance & Risk Management
- Internal Management Reviews
- KPI & data quality
- Benchmarking
- Programme and Project Management

External Review/ Assurance

- External Audit plans, letters and reports
- Inspection reports
- Peer reviews
- External Commissioned reviews
- Ombudsman

Corporate Assurance

- Consultation/ complaints/ feedback
- Scrutiny process
- Audit Committee
- Statutory Officers
- Legal Services
- The Executive
- Equality Impact Assessments
- Codes of Conduct

Set out the arrangements for compilation and approval of the Annual Governance Statement 2023/24	
Audit Committe	Annual

Review progress made against any significant issues included in the 2022/23 Annual Governance Statement	
Audit Committee	Ongoing

Consideration of significant issues for 2023/24 Annual Governance Statement	
Corporate Leadership Team, Statutory Officers & Finance Business Partners	Ongoing

Approval of 2023/24 Annual Governance Statement

Leader, Chief Executive and Audit Committee - September 2024

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North Somerset Council

Report to the Audit Committee

Date of Meeting: 25th January 2024

Subject Of Report: Audit Plan – Audit Committee Consultation

Town or Parish: None

Officer/ Member Presenting: Peter Cann - Audit West

Key Decision: No

Recommendations

The Audit Committee is asked to:

- Comment on any areas or themes they would like to be considered in relation to the Internal Audit Plan for 2024/25.
- Note the intention to keep the plan under regular review, including a six-month progress assessment, in order to prioritise resources as required.

1. Summary of Report

This report updates the Audit Committee on the methodology used to create the Internal Audit Plan and asks for comments on areas or themes they would like to be considered within the plan for 2024/25.

2. Policy

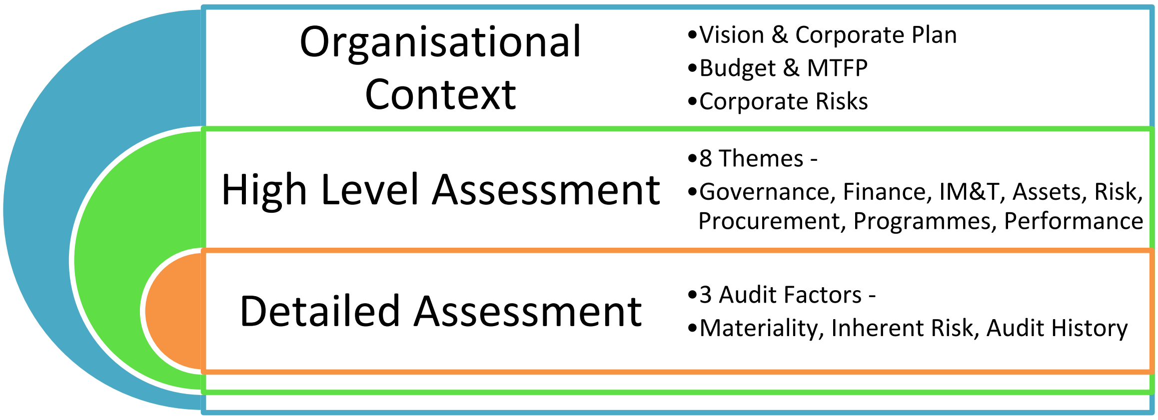
The work of the Internal Audit Service is to provide independent assurance to the council's senior officers and members that governance, risk management and controls are sufficient in ensuring delivery of the council's objectives.

3. Details

3.1 The planning process is based on the fundamental requirement that the audit plan proposed will deliver sufficient work to enable the Head of Internal Audit to independently assess the internal control framework and give a reasonable assurance opinion at the end of each year.

3.2 The model used to develop the audit plan – the Reasonable Assurance Model - has regularly been described to the Committee in detail. It was created and adopted in conjunction with a number of other councils in the South West and its approach won a Public Finance award.

3.3 The outline of the model is as follows with the key elements in the middle section which introduce a high-level assessment of themes based on good governance.



3.4 A key part of the planning process is therefore extensive stakeholder consultation. Conversations in this regard usually take place between December to March and discussions will therefore take place with the following officers/ groups up until the end of March:

- Section 151 Officer
- Finance Business Partners & Head of Finance
- Directorate Leadership Teams
- Statutory Officers
- Audit Committee

3.5 <u>Rolling Plan Review</u>

3.5.1 During recent years and looking back to 2020/21 in particular, members may recall that some changes to planned work were required in order to redirect audit resources to unforeseen issues arising from the then emerging COVID-19 pandemic. At approximately six months in to the 2020/21 plan, it was considered that the plan should be rebased for the rest of that financial year as a better understanding had been gained of the impact of COVID-19 and how resources should be subsequently prioritised. This was discussed and agreed at the time with the Audit Committee.

3.5.2 Whilst only small adjustments have since been required to audit plans for subsequent years, the Internal Audit Service have continued to ensure a fluid approach to planned audit work. Therefore, whilst the usual consultation process will follow and a full-year audit plan will initially be produced to cover the period 1st April 2024 – 31st March 2025, the plan will be kept under continual review and adjusted to cover any further unforeseen requirements over the first six months. A review of the annual plan at the six-month stage will then take place, if necessary, in order to adequately prioritise and resource the second half of the financial year.

3.6 <u>Audit Committee - Consultation & Input</u>

3.6.1 The Audit Committee is a key stakeholder and ultimately approve the Audit Plan. Therefore, the purpose of the report is to obtain views and feedback on areas which the planning process can consider and take account of before it is finalised in early March.

3.6.2 The Chartered Institute of Internal Auditors has published a report which tracks the risks for 2024 as highlighted by organisations and to which should be taken into account when preparing their audit plans.

The top risk areas from the report which are particularly relevant to the public sector are detailed below. This list may assist the committee as a point of reference to help understand where they feel audit coverage may be beneficial.

- Cybersecurity and data security
- Human capital, diversity and talent management
- Changes in laws and regulations
- Macroeconomic and geopolitical uncertainty
- Business continuity, operational resilience, crisis management & disaster response
- Digital disruption, new technology and AI
- Climate change and environmental sustainability
- Financial risk
- Organisational governance and corporate reporting
- Fraud, Bribery and the criminal exploitation of disruption

4. Consultation

In developing and delivering the Annual Audit Assurance Plan the Internal Audit Service is consulting widely with officers and members. Ongoing consultation will continue with the Audit Committee throughout the year after the plan has been approved.

5. Financial Implications

There are no direct financial implications from this report, however finance is considered throughout the planning process including consideration of the Budget and MTFP.

6. Risk Management

Significant risks to the council arising from an ineffective Internal Audit Service include lack of internal control, failures of governance and weak risk management. Specific risks include supplementary External Audit Fees, undetected fraud and inadequate coverage. Internal Audit assists the council in identifying risks, improvement areas and recommending good practice. Directorate and Strategic Risk Registers are also reviewed when developing the internal audit plan.

7. Legal Powers and Implications

Accounts & Audit Regulations set out the expectations of provision of an Internal Audit service. This is supported by S151 of the Local Government Act and CIFPA Codes of Practice and the IIA professional standards for delivery of an adequate Internal Audit Service. Implications of not providing this service may include qualification of the Accounts, increase in External Audit fees, potential rise in fraud and corruption and misappropriation of assets and resources.

8. Climate Change & Environmental Implications

The plan process will consider key risks (& opportunities) which will directly or indirectly include focus on Climate Change and report back on whether assurances can be given on the delivery of the organisations plan to mitigate the risk in this area.

9. Equality Implications

Embedded within the audit process is consideration of compliance with statutory guidance and regulations which includes those relating to equality and diversity.

10. Corporate Implications

Failure to deliver the agreed Annual Assurance Plan may result in an inability to provide assurance to officers and members of the council's corporate governance.

11. Options Considered

Audit Methodology is driven by professional standards and legislative requirements and the model created subjected to external assessment. The plan itself is subject to wide consultation in order to ensure sufficient options and approaches have been considered.

AUTHOR

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BACKGROUND PAPERS

Annual Audit Assurance Plan 2023/24 Audit Committee March 2023

Grant Thornton

Auditor's Annual Report on North Somerset Council

2022/23

November 2023

Contents

We are required under Section 20(1)(c) of the Local Audit and Accountability Act 2014 to satisfy ourselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources. The Code of Audit Practice issued by the National Audit Office (NAO) requires us to report to you our commentary relating to proper arrangements.

We report if significant matters have come to our attention. We are not required to consider, nor have we considered, whether all aspects of the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources are operating effectively.

The contents of this report relate only to those matters which came to our attention during the conduct of our normal audit procedures which are designed for the purpose of completing our work under the NAO Code and related guidance. Our audit is not designed to test all arrangements in respect of value for money. However, where, as part of our testing, we identify significant weaknesses, we will report these to you. In consequence, our work cannot be relied upon to disclose all irregularities, or to include all possible improvements in arrangements that a more extensive special examination might identify. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting, on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

Executive summary

Value for money arrangements and key recommendation(s)

Under the National Audit Office (NAO) Code of Audit Practice ('the Code'), we are required to consider whether Swindon Borough Council (the Council) has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

Auditors are required to report their commentary on the Council's arrangements under specified criteria and 2022/23 is the third year that we have reported our findings in this way. As part of our work, we considered whether there were any risks of significant weakness in the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources. Where we identify significant weaknesses in arrangements, we are required to make recommendations so that the Council may set out actions to make improvements. Our conclusions are summarised in the table below.

Criteria	2022/23 Risk assessment	2021/22 Auditor judgement on arrangements		2022/23 Auditor judgement on arrangements	
Financial sustainability	No risks of significant weakness identified.	G	No significant weaknesses in arrangements identified, or improvement recommendations made.	A	No significant weaknesses in arrangements identified, but one improvement recommendation made.
Governance	No risks of significant weakness identified.	A	No significant weaknesses in arrangements identified, but two improvement recommendations made.	G	No significant weaknesses in arrangements identified, or improvement recommendations made.
Improving economy, efficiency and effectiveness	No risks of significant weakness identified.	A	No significant weaknesses in arrangements identified, but two improvement recommendations made.	A	No significant weaknesses in arrangements identified, but one improvement recommendation made.

G	No significant weaknesses in arrangements identified or improvement recommendation made.
A	No significant weaknesses in arrangements identified, but improvement recommendations made.
R	Significant weaknesses in arrangements identified and key recommendations made.

Executive summary (continued)

Financial sustainability

Our work has not identified evidence of significant weaknesses within the arrangements on how the Council plans and manages its resources to ensure it can continue to deliver its services. However, we have raised three improvement recommendations. The first two are in relation to monitoring delivery of capital expenditure programme and strengthening the link between strategic priorities and the capital programme, specifically the capital programme could be categorised by outcomes identified within particular Council Plan outcomes. Thirdly, there should be formal reporting to Executive Committee members on the sensitivity analysis and the scenario planning that is undertaken on key assumptions and estimates as part of the development of the annual budget and Medium-Term Financial Plan. See page 15 for more detail.

Governance

Our work has not identified evidence of significant weaknesses within the arrangements in place for how the Council makes informed decisions and properly manages its risks. Strategic risks are included within the overall risk assessment framework and are monitored and managed through the corporate risk registers. We consider that appropriate arrangements are in place to ensure all relevant information is provided to decision makers before major decisions are made. The Council has appropriate arrangements in place to monitor compliance with legislation and regulatory requirements.

Improving economy, efficiency and effectiveness

Our work has not identified evidence of significant weaknesses and the Council has appropriate arrangements in place in its oversight of economy, efficiency and effectiveness. We have identified an improvement recommendation in relation to how the Council might pay close attention to this delivery of the action plan arising from recommendations in both Ofsted inspections; doing what it has agreed to do, on time, can help to rebuild complainants' trust and confidence after things have gone wrong. See page 23 for more detail.

Financial Statements opinion

We have completed our audit of your financial statements and issued an unqualified audit opinion on 2 October 2023, following the Audit Committee meeting on 21 September 2023. Our findings are set out in further detail on pages 31 to 32.

Use of auditor's powers

We bring the following matters to your attention:

	2022/23
Statutory recommendations Under Schedule 7 of the Local Audit and Accountability Act 2014, auditors can make written recommendations to the audited body which need to be considered by the body and responded to publicly.	We did not make any written recommendations under Schedule 7 of the Local Audit and Accountability Act 2014.
Public Interest Report Under Schedule 7 of the Local Audit and Accountability Act 2014, auditors have the power to make a report if they consider a matter is sufficiently important to be brought to the attention of the audited body or the public as a matter of urgency, including matters which may already be known to the public, but where it is in the public interest for the auditor to publish their independent view.	We did not issue a public interest report.
Application to the Court Under Section 28 of the Local Audit and Accountability Act 2014, if auditors think that an item of account is contrary to law, they may apply to the court for a declaration to that effect.	We did not make an application to the Court.
Advisory notice Under Section 29 of the Local Audit and Accountability Act 2014, auditors may issue an advisory notice if the auditor thinks that the authority or an officer of the authority: • is about to make or has made a decision which involves or would involve the authority incurring unlawful expenditure, • is about to take or has begun to take a course of action which, if followed to its conclusion, would be unlawful and likely to cause a loss or deficiency, or • is about to enter an item of account, the entry of which is unlawful.	We did not issue any advisory notices.
Judicial review Under Section 31 of the Local Audit and Accountability Act 2014, auditors may make an application for judicial review of a decision of an authority, or of a failure by an authority to act, which it is reasonable to believe would have an effect on the accounts of that body.	We did not make an application for judicial review.

Securing economy, efficiency and effectiveness in the Council's use of resources

All councils are responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness from their resources. This includes taking properly informed decisions and managing key operational and financial risks so that they can deliver their objectives and safeguard public money. The Council's responsibilities are set out in Appendix A.

Councils report on their arrangements, and the effectiveness of these arrangements as part of their annual governance statement.

Under the Local Audit and Accountability Act 2014, we are required to be satisfied whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

The National Audit Office's Auditor Guidance Note (AGN) 03, requires us to assess arrangements under three areas:

Financial sustainability

Arrangements for ensuring the Council can continue to deliver services. This includes planning resources to ensure adequate finances and maintain sustainable levels of spending over the medium term (3-5 years).

Governance

Arrangements for ensuring that the Council makes appropriate decisions in the right way. This includes arrangements for budget setting and management, risk management, and ensuring the Council makes decisions based on appropriate information.

Improving economy, efficiency and effectiveness

Arrangements for improving the way the Council delivers its services. This includes arrangements for understanding costs and delivering efficiencies and improving outcomes for service users.

Our commentary on the Council's arrangements in each of these three areas, is set out on pages 7 to 25.

In addition to our financial statements audit work, we perform a range of procedures to inform our value for money commentary:

- Review of Council, Cabinet and committee reports
- Regular meetings with senior officers
- Interviews with other members and management
- Attendance at Audit Committee
- Considering the work of internal audit
- Reviewing reports from third parties including Ofsted
- Reviewing the Council's Annual Governance Statement and other publications

The current LG landscape

National context

Local government in England continues to face significant challenges as a sector. These include a high level of uncertainty over future levels of government funding, alongside delays to the Government's plans for reform of the local government finance system, impacting on medium-term financial planning. This is also a time of generationally significant levels of inflation – the UK inflation rate was 7.8% in April 2022, rising to a 41-year high of 11.1% in October 2022, then reducing to 10.1% in March 2023. As at October 2023 it had fallen further back to 4.7%, but is still higher than in recent years and the last peak of 4.8% in September 2008. Inflation levels put pressure on councils' revenue and capital expenditure, as well as the associated cost of living crisis impacting on local communities and businesses, leading to an increase in demand for council services such as children with special education needs with associated transport costs, debt advice, housing needs, and mental health, as well as impacting on some areas of council income such as car parking and the collection rates of council tax, business rates and rents. This follows a significant period of funding reductions by Government (2012 to 2017) and the impacts of Brexit and the COVID-19 pandemic which, for example, have contributed to workforce shortages in a number of council service areas, as well creating supply chain fragility risks.

The local government finance settlement for 2023/24 was better than many in the sector anticipated demonstrating an understanding by Government of the financial challenges being faced by the sector. However, the Local Government Association, in July 2023, estimated that the costs to councils of delivering their services will exceed their core funding by £2bn in 2023/24 and by £900m in 2024/25. This includes underlying cost pressures that pre-date and have been increased by the pandemic, such as demographic pressures increasing the demand for services such as social care and homelessness.

Over the past decade many councils have sought to increase commercial activity as a way to generate new sources of income which has increased the nature of financial risk, as well as the need to ensure there is appropriate skills and capacity in place to manage such activities.

Local government is coming under an increased spotlight in terms of how the sector responds to these external challenges, including the Government establishing the Office for Local Government (Oflog) and there has been an increase in the number of councils who have issued a Section 114 Notice, or are commenting on the likelihood of such an action, as well as continued Government intervention at a number of councils.

There has also been an increase in the use of auditors using their statutory powers, such as public interest reporting and statutory recommendations. The use of such auditor powers typically derive from Value for Money audit work, where weaknesses in arrangements have been identified. These include:

- a failure to understand and manage the risks associated with commercial investments and council owned companies
- a failure to address and resolve relationship difficulties between senior officers and members
- significant challenges associated with financial capability and capacity
- a lack of compliance with procurement and contract management processes and procedures
- ineffective leadership and decision-making.

Value for Money audit has an important role in providing assurance and supporting improvement in the sector.

The current LG landscape (continued)

Local context

The Council provides a full range of local government services including housing, waste collection and disposal, education, social services, libraries and planning. It is also a billing authority for collection of council tax and business rates

The Council is elected every four years, electing a total of 50 councillors in 20 single-member wards and 15 two-member wards. Since the first election to the unitary authority in 1995, the Council has either been under Conservative party control, or no party has held a majority. The Conservatives gained a majority at the 2007 election and retained control until the 2019 election. Since the May 2023 local elections, there has been a joint Conservative and Liberal Democrat administration. In 2023, this approach was reinforced and the Council Partnership administration of Liberal Democrat, Labour, Green and independent councillors was refreshed.

The Council Plan priorities include providing greater support for local businesses and a reduced dependence on long-distance travel. In addressing the challenge of providing housing, health, jobs and infrastructure for current and future generations, the Council is seeking to make use of technology and sustainability. The Council Plan highlights the ambition of the Council to develop living and working spaces, with minimal environmental impact, offering access to community, education, jobs, leisure and travel.

Financial sustainability

We considered how the Council:

- identifies all the significant financial pressures that are relevant to its short and medium-term plans and builds them into its plans
- plans to bridge its funding gaps and identify achievable savings
- plans its finances to support the sustainable delivery of services in accordance with strategic and statutory priorities
- ensures its financial plan is consistent with other plans such as workforce, capital, investment and other operational planning which may include working with other local public bodies as part of a wider system
- identifies and manages risk to financial resilience, such as unplanned changes in demand and assumptions underlying its plans.

Short and medium term financial planning

The Council's 2022/23 budget (agreed by the Executive and Full Council in February 2022) set net revenue expenditure at £185.475m. This was based on a council tax increase of 2.99%, comprising 1.99% for the basic amount of council tax and a specific adult social care precept of 1%, in accordance with Schedule 5 of the Localism Act 2011 and therefore did not trigger the requirement for a local referendum.

Key assumptions in the approved 2022/23 budget included, a new grant of £626k allocated to cover the first year of the social care reforms, specifically aimed at sustaining the market and providing a fair price for care. The Council's spending plans have also been adjusted by this sum and funding was ring-fenced to ensure that spending plans meet the relevant criteria. Further sums are expected in later years to fund changes associated with other reform measures, such as the 'care-cap', although no details have been provided at this time. The budget confirmed the values and distribution methodology for existing social care grants, with the council's share reaching £8.095m in 2022/23 which is slightly higher than the previous forecast and will be maintained and included within future budgets. A further year of the new homes bonus grant, on top of the final legacy payments, the council's forecasts reflected the legacy payment and so the resources budget was updated to include the latest one-off award of £1.5m in 2022/23, reversing in 2023/24. This was ring-fenced and used as one-off fund to support capital planning, feasibility and investment proposals. A Services grant (lower tier) – a new allocation of £224k was awarded to the council for 2022/23 which was not included within the previous forecasts. This grant is a one-off and has been included for 2022/23 only.

The Medium Term Financial Plan (MTFP) (2022-2025) commentary on significant or notable areas highlighted the assumptions made included cost and demand pressures in the Council's adult social care budgets which are significant and not fully funded by the Government. The MTFP commentary includes the measures the Council has put in place to manage the costs pressures and manage demand. For example, the MTFP highlighted the introduction of 'cost and volume' models in areas such as social care, waste services and home to schools' transport, which are linked to projected numbers and volumes of activity or service provision, with the costs that are paid to providers. Planned increases in service spending total £8.7m, with £5.5m relating to increased care provider costs driven by a 6.6% increase in the National Living Wage which was announced by the Government in the Autumn of 2021, plus increases in employer National Insurance contributions for the Health and Social Care Levy. Demographic pressures were estimated to lead to increased costs of £1.5m; these relate to the increasing numbers of older people needing services and the number of children with complex needs moving into adulthood.

By way of example, population estimates indicate that there will be around 1,000 more people aged 75 and over in North Somerset in 2022/23 and more than 20 young people who reach 18 that will need adult social care support. Planning growth in spend in Children's Services totals £2.1m and is largely split into two categories – existing cost pressures and investment to deliver service improvements. Additional growth of £460k is needed within the budget for next year so that the council can continue to support families with disabled children. Other new investment of £1.1m is being included within the budget to support the council's improvement plan for social care and children with special educational needs and disabilities. Within the Council Corporate Services and Place Directorate additional resources were allocated to address specific service-related issues such as the Ash-Dieback programme, investment in Information and Communications (ICT), cyber security and capacity in the council's website and communications services. Other budgeted expenditure increases related to increased costs pressures, such as insurances, and sustained reductions in income budgets.

The 2022/23 budget report included climate related implications within the revenue expenditure budget and these are integrated into the budget in ways in which services are being considered and delivered. For example, the budget reflects provision for increased energy costs however, the procurement activity associated with assessing what types of energy to purchase and where to buy it from, now also include objectives linked to achieving 'greener' outcomes. Similar considerations were taken into account when re-procuring the parks and Streetscene contract, as re-wilding and other environmental impacts were assessed. The Council also has the ability to influence the environmental impacts when investing in services and projects, further details relating to planned investments for next year are included in the Council annual Capital Strategy report.

Financial sustainability (continued)

Short and medium term financial planning (cont.)

The Council 2022/23 budget incorporates the Council's involvement with North Somerset Environment Company Ltd (NSEC). NSEC is a wholly owned subsidiary of the Council, incorporated on 26th October 2020, with a share capital of one ordinary share of £1. The principal activity of the company is the provision of waste and recycling services for the Council.

The budget for 2022/23 also details the Council's involvement with the North Somerset Bus Service Improvement Plan (BSIP) which allocates capital funding awards of £47.98m allocated to the Council, and indicative revenue funding award of £57.51m allocated jointly to the West of England Combined Authority and the Council. The proposed outline BSIP delivery commissioning plan for delivery of the Bus Service Improvement Plan works programme across North Somerset commencing in autumn 2022.

2022/23 financial performance

The 2022/23 budget out-turn report (to Executive in June 2023) highlighted the council delivered a small under spend of £418k, or 0.23% of the net revenue budget. Savings plans were achieved in full, with £4.6m delivered which was higher than the planned budget of £4.2m. The council's general reserve balance at the start of the year was £9.1m, which equated to 5.25% of the original net budget of £185.5m. This reserve is not held to fund spending priorities, instead it treated as a working balance to cover unforeseen or unavoidable financial risks.

There was a potential requirement to use the general fund reserve for any residual revenue overspend remaining at the end of the financial year. However, as the Council has achieved an under spend on the revenue budget for 2022/23 the closing balance on the reserve increased to £10.16m, or approximately 5.48% of the net revenue budget.

The 2022/23 Capital Outturn report (to Executive June 2023) highlighted the Council's overall programme (2022/23 to 2026/27) totals £391.2m, £109.9m of which relates to the 2022/23 financial year. The Council spent £66.5m during 2022/23, which equated to 61% of budget for the year, the Council has also placed commitments for schemes totalling a further £15.7m .

This is a significant increase in the scale of capital delivery over previous years, and given the Council's recent track record of significantly under spending on the capital programme, we have made an improvement recommendation on page 15 relating to monitoring of capital expenditure to address the under-delivery of the capital expenditure programme.

Table 1 (below) highlights the Council's performance on key financial performance metrics 2021/22 and 2022/23.

Table 1 – Key Financial performance	2022/23	2021/22
Planned revenue expenditure	£185.5m	£176.7m
Actual revenue expenditure	£185.1m	£176.0m
Planned capital spend	£109.9m	£94.4m
Actual capital spend	£66.5m	£45.4m
Planned savings target	£4.2m	£7.5m
Actual savings delivered	£4.6m	£7.5m

Financial sustainability (continued)

2022/23 financial performance (cont.)

2022/23 Treasury Management performance reported to Audit Committee in September 2023 highlighted, following a series of bank base rate increases during 2022/23, gross interest income earned on all investments was £3.35m, against a budget of £0.69m. Investment returns - the average rate of investment return for cash deposit type investments managed by the Council for 2022/23 - was 1.62% and returns of 4.32% being achieved on external pooled fund investments. The Council's treasury strategy contained a borrowing requirement of £49m for 2022/23. Changes to capital forecasts have been reported through the corporate monitoring process and as of 31 March 2023, the council had not drawn down any further external borrowing. £6.8m of borrowing was repaid, as planned, during 2022/23.

Identifying savings

MTFP savings are part of the financial reporting framework. Savings are considered and discussed on a regular basis between the Executive Committee members, the Service Director and the Chief Executive. The section 151 Officer is also part of the meeting and assists members talk through the savings and assess any further implications.

Budget proposals for savings are supported by an equality impact assessment (EIA). Draft EIAs were published on the Council's website in December 2021 and a stakeholder discussion group was held in January 2022 to share information around medium impact EIAs.

The Budget and Council Tax Report 2022/23 noted that £4.2m of agreed budget savings and cost reductions were required to be delivered. This included savings in Adults of £1.14m, Childrens of £0.61m, Corporate Services of £0.70m and Place Operations of £1.28m.

Based on the Council's reserves position and MTFP, we consider the Council has sufficient reserves to act as a contingency for the current MTFP if the Council fails to fully identify the required savings. Our review of recent years savings target delivery highlights the Council has a good track record for delivery of savings targets.

Financial planning and strategic priorities

The Council's financial planning approach sets out the cost of delivering core statutory services as distinct from discretionary areas of spend. Financial planning reports which support the budget and MTFP highlight all spend is prioritised towards the delivery of core services and achievement of Council Plan priorities. Responsible budget management underpins the Council's strategic objective of consistently making the best use of all available resources as well as providing focus for its change programmes.

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The MTFP is the framework for how the Council plans to use its financial resources to deliver activity on the Councils outcomes. The Council considered the MTFP one of three key strategic documents: linking/ interconnecting the MTFP to -the Corporate Plan and the People strategy, the other two key strategic documents. We are satisfied the Council MTFP is appropriately integrated with the Corporate plan acting as the foundation to deliver the vision and priorities within it and the People strategy, which is the framework to develop the workforce to achieve Council Priorities

The Council's priority outcomes are set out in the Council Corporate Plan 2020 - 2024. The outcomes which drive the work of the Council, and the strategic planning process are:

- Making North Somerset a thriving and sustainable place,
- A Council which empowers and cares about people,
- An open and enabling organisation.

£790m of cash-flows were managed during the 2022/23 period; this is broadly comparable with the equivalent period in 2021/22 (£789m). Non-treasury management activity relating to commercial investments provided an annual yield of 2% in 2022/23 before a contribution to a reserve of £1.1m to smooth annual fluctuations on the council's revenue budget if needed.

The 2022/23 Capital Strategy (presented to the Executive in February 2022) highlighted new capital investment requirements through to 2025/26, resulting in an increase to the capital programme of £38.7m in 2022/23 for a range of new investments. These included in relation to children and young people, delivering better basic services, investing in communities and tackling the climate emergency. The revised borrowing impact within the capital programme was £94.3m for approved schemes to 2022/23 the Council highlighted this could rise to £138.0m by 2026. The new capital schemes approved set out in this report require additional borrowing of £6.3m. There is appropriate commentary explaining the affordability of increases to the resulting estimated net revenue impact will be and this has been included in the MTFP.

We have identified that there is an opportunity to strengthen the link between strategic priorities and the capital programme, and the capital programme could be further categorised by Council Plan outcomes. This would demonstrate clearly how the Council is delivering their Council Plan outcomes through the capital programme, and we have made an improvement recommendation relating to this on page 15 regarding this.

Financial sustainability (continued)

Managing risks to financial resilience

The MTFP set outs key risks to delivery and the actions to mitigate each risk identified. The MTFP was presented and discussed by the Executive in February 2022 allowing for scrutiny and questioning (before presentation to full Council). The MTFP highlights the Council's reserves form an important role in managing uncertainty, including demand pressures in children's and adult social care, and wider demographic pressures on services. Inflation is a key risk, in particular energy prices and supply chain pressures.

The impact of inflation on actual expenditure compared to budget is appropriately highlighted in the 2022/23 out-turn report, which provides detailed budget performance analysis. The Council takes appropriate action to update financial plans to reflect changes in government policy. Where required, the Council has sufficient provisions in place to consider the impact of legal and regulatory proceedings

The Council have appropriate arrangements in place to monitor these budget risks and review and update the MTFP where required. The potential impact of changes to various estimates and assumptions is discussed with the Executive as part of the briefing process in the development of the budget. However, the impact of changes of various estimates and assumptions is not formally reported to members.

In prior years we identified that management had not included formal reporting to Cabinet members on sensitivity analysis and scenario planning, undertaken on key assumptions and estimates, as part of the development of the annual budget and MTFP. This provides transparency on the sector wide uncertainties the council is subject to and the potential impact of these on its financial sustainability. Our review of arrangements in 2022-23 noted that scenario planning and sensitivity analysis was included as part of the budgeting process but was not included in formal reporting to members. This was in line with the prior year recommendation as reported on page 24. We have continued to review arrangements, up to the date of issuing of the report and have noted that scenario planning is included within the 2023-24 budget process. We will assess the robustness of this analysis within our review of the 2023-24 arrangements. We consider that the prior year recommendation has been addressed.

Financial sustainability (continued)

Reserves and risk mitigation

Section 25 of the Local Government Act 2003 requires the Section 151 Officer to report on the robustness of estimates within the budget and the adequacy of levels of reserves. As part of the 2022-23 budget the Section 151 officer recommended the level of General Fund (GF) balance should equate to between 4% and 6% of the authority's revenue budget. In 2022/23 due to the surplus outturn position for 2022/23 the Councils level of General Fund balance was increased to £10.16m (5.48% of net revenue budget) at the year end. Due to the uncertainties affecting local authority budgets the Chief Financial Officer has noted that the minimum level of reserves is £9m with £11m being the ideal.

The key issues highlighted by the Section 151 Officer in the Section 25 report included:

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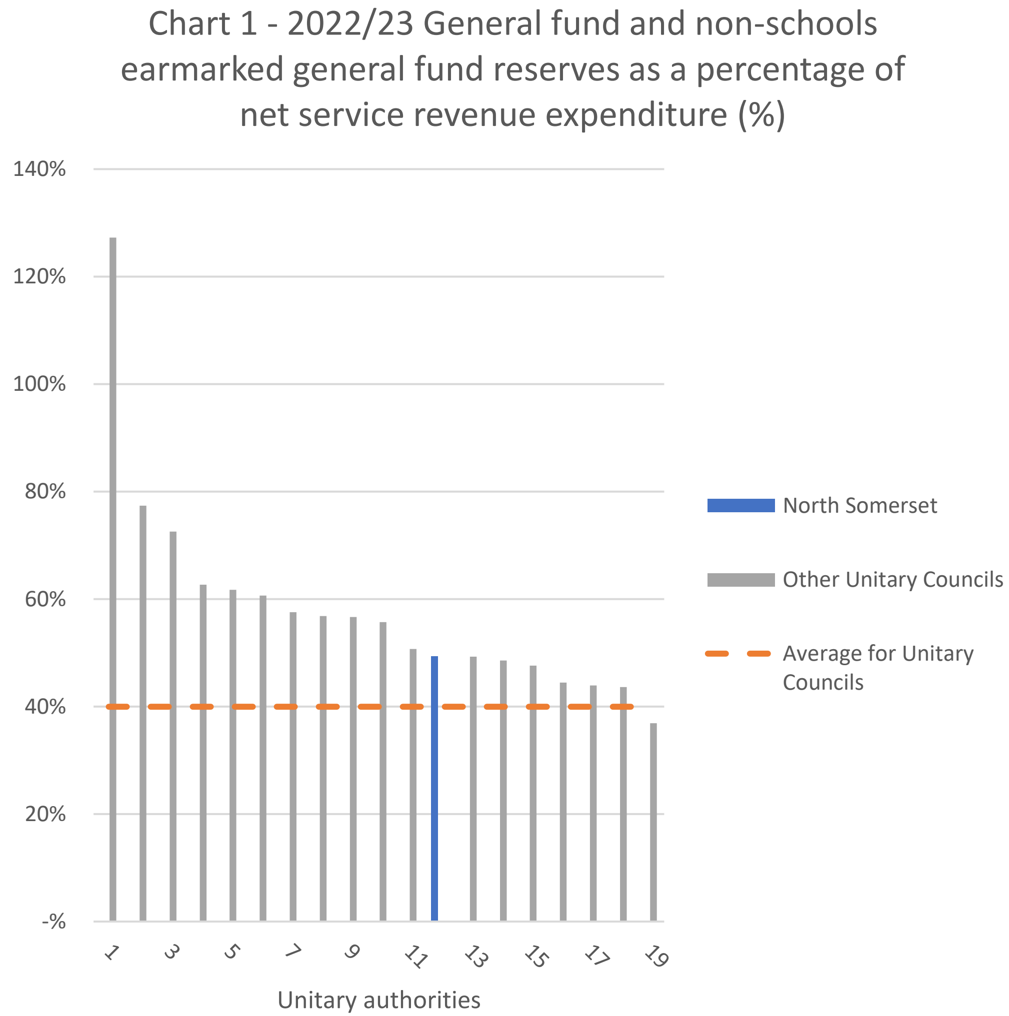
- Continuation of financial uncertainties including Covid-19.
- Potential unforeseen and material remediation works to infrastructure assets.
- Other material contract failures.
- The increasing cost and demand pressures for adult and children social care.
- The risk surrounding the non-delivery of savings and exceeding investment proposals with the budget.
- The extreme financial issues for the public sector arising from the prevailing and continuing national and local conditions.

The Section 151 Officer confirmed that the 2022/23 budget was prepared robustly and was achievable. We are satisfied the level of reserves appear adequate given known current developments and challenges and is in line with the Council stated objective. The budget for 2022-23 highlighted the following – "*At the end of 2022/23 it is projected that the General Fund Balance is forecast to be £9.744m, or 5.25% of the council's net revenue budget which is within the acceptable range.*" *As already noted, the Council reserve position at the end of 2022/23 exceeded this target.*

Balancing the 2022/23 budget was not dependent on the one-off use of reserves. There is no evidence that that the Council has depleted the level of revenue reserves to an unsustainable level. The unallocated General Fund balance has increased to £10.16m having been maintained at £9.05m since 2018-19. Chart 1 opposite shows the Council's position relative to other benchmarked authorities for the General fund measure is above average.



Financial governance

Annual budget setting

The Council has an established process for developing its annual budget and MTFP. The development of the budget commences with the rolling forward of the budget from the prior year. The budget is updated to reflect any known permanent changes to funding, including new grants, latest Council Tax base data and Business Rates. Prior year assumptions are reviewed, including inflation rates and Council Tax base. Updates are then made to reflect new savings proposals, existing savings delivery, service pressures, changes to sources of funding announced within the spending review, changes to service fees and charges and the Council tax base. The Budget is frozen to prepare the February Executive Report.

The Council's MTFP covers a rolling three-year period. A report was brought to Executive in December 2021 which outlined the approach to updating the MTFP for 2022/23. The MTFP update report contained the financial planning assumptions for the period of the new three-year MTFP set within this Corporate Plan. It updates the 2022-2025 Budget Planning position and proposed the approach that will be taken to deliver the savings required to achieve a balanced budget over the three-year period. The report is clear on the challenges facing the Council, which include the ongoing impact of the pandemic, pressure on services and uncertainty about central government funding.

The 2022/23 Budget and MTFP to 2022- 2025 was agreed by Executive (and subsequently Full Council) in February 2022. We consider there to be a good level of engagement from budget holders, divisional leadership and executive leadership in the annual budget setting process. The Council has arrangements in place to recognise, assess, and re-evaluate the impact of changes in expenditure drivers, including pay inflation.

Risks are incorporated into the MTFP, there is a section of the MTFP highlighting key risks to delivery of the MTFP and the actions to mitigate each risk identified.

Table 2 (opposite) highlights key 2023/24 budget targets agreed in February 2023. The Council has a good track record of deliver savings to targets, we have made an improvement recommendation earlier in this report relating to delivery of capital programme expenditure.

Table 2 - 2023/24 key financial performance measures	2023/24
Planned revenue expenditure	£202.1 m
Planned capital spend	£112.8 m
Planned savings	£10.4 m
Planned savings as a % of income	5.15%

Budgetary control

The Council has appropriate systems in place for oversight of the budget. The Finance Department engages at least monthly with budget holders and there is monitoring at a service, directorate and corporate level. The Council has detailed in year oversight of the budget at a high level, with bi-monthly budget monitoring reports taken to Executive. These reports include outturn against budget and explanations for underspend/ overspends against budget at a directorate level. Any proposed revisions to the budget are also communicated through this report. There is clear reporting on the forecast outturn and the impact on useable reserves. A quarterly update is also provided against the Capital Programme, with revisions also communicated. We are satisfied that timely and accurate financial monitoring information is provided to budget holders.

Conclusion

The Council has a track record of appropriate financial management arrangements. The Council understands the financial risks which it faces and manages these risks by maintaining an appropriate level of reserves in accordance with its stated reserves objectives in the MTFP.

Overall, we are satisfied that the Council has appropriate arrangements in place to manage the risks it faces to financial resilience. We have not identified any risks of significant weakness but have identified one opportunity for improvement, detailed on page 15.

Improvement recommendations

Improvement Recommendation 1	The capital programme supports the delivery of strategic priorities. To strengthen the link between strategic priorities and the capital programme, the capital programme could be categorised by outcomes identified within particular Council Plan outcomes. This would demonstrate clearly how the Council is delivering their Council Plan outcomes through the capital programme. Allied to this the Council should continue to closely monitor delivery of the capital programme to highlight any slippage and provide an update for management actions to address the under delivery.
Improvement opportunity identified	This would demonstrate clearly how the council is delivering their Council Plan outcomes through the capital programme.
Summary findings	The Capital Strategy (presented to Executive February 2022) highlighted capital strategy and new capital investment requirements through to 2025/26. This included an increase to the capital programme of £38.7m in 2022/23 for a range of new investments relating to children and young people, delivering better basic services, investing in communities and tackling the climate emergency. It also included an assessment of the revised borrowing impact within the capital programme of £94.3m for approved schemes to 2022/23, which could rise to £138.0m by 2026 The new approvals set out in this report require additional borrowing of £6.3m. The resulting estimated net revenue impact will be built into the MTFP. The 2022/23 Capital Outturn report to Executive June 2023 highlighted the council's overall programme totals £391.2m, £109.9m of which relates to the 2022/23 financial year. The capital summary shows that the council spent £66.5m during 2022/23, which equated to 61% of budget for the year, although has placed commitments for schemes totalling a further £15.7m which would increase the spending to 75% of the budget. This is a significant increase in the scale of capital delivery over previous years.
Criteria impacted	Financial sustainability
Auditor judgement	Clear detailed links highlighting how planned capital projects link to the Council Plan would enable members make informed decisions and challenge Capital Strategy assumptions to help ensure forecasts remain accurate. Our work has enabled us to identify a weakness in arrangements which we do not consider to be significant but have raised a recommendation to support management in making appropriate improvements. Progressing the actions management has identified to address the recommendations made will support the Council in addressing the improvements identified from our work. We consider that the timescales provided by management are appropriate and encourage the Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place. The range of recommendations that external auditors can make is explained in Appendix B.
Management comments	The Council have taken steps to improve the governance arrangements and clarity of financial monitoring to members throughout 2022-23 and this process is now embedding and has been recognised by both the chairs of the audit committee and PCOM scrutiny. Significant variances in the capital budget are now reported in the Executive budget monitoring reports, including narrative. We recognise that the council is experiencing significant slippage in its capital programme, in common with many other local authorities, and steps are being taken to improve the allocation of budgets to align with deliverability. We will ensure that capital reporting for 2024-25 recognises the link to our new Corporate Plan.

Governance

We considered how the Council:

- monitors and assesses risk and gains assurance over the effective operation of internal controls, including arrangements to prevent and detect fraud
- approaches and carries out its annual budget setting process
- ensures effective processes and systems are in place to ensure budgetary control; communicate relevant, accurate and timely management information (including non-financial information); supports its statutory financial reporting; and ensures corrective action is taken where needed, including in relation to significant partnerships
- ensures it makes properly informed decisions, supported by appropriate evidence and allowing for challenge and transparency
- monitors and ensures appropriate standards, such as meeting legislative/regulatory requirements and standards in terms of staff and member behaviour (such as gifts and hospitality or declaration of interests) and where it procures and commissions services.

Risk management and internal controls

The Strategic Risk Register (SRR) is clearly set out, with a risk owner, concise description and key controls to manage the risk. The Council has a current Risk Management Policy (September 2022), Process Guide and Toolkit to ensure consistent scoring of risks across all Directorates. The SRR has appropriate detail highlighting the actions in place to mitigate and manage all risks identified. The Council provides appropriate training on risk management. The Council's Risk Appetite was unchanged throughout 2022/23. As of September 2023, there are eleven risks that have been identified and included on the SRR risk register of which six have a residual high-risk rating. These are:

- Coastal flooding which negatively impacts on people, businesses and communities
- Cyber-attack which damages the infrastructure of the Council
- Failure by the Council to meet the 2030 net zero target
- An inability of the Council to balance its budget
- An inability of the Council to deliver capital projects within the approved resource envelope
- The condition of the corporate estate/assets pose an increasing financial, operational and reputational risk

Of the remaining five there are three that are considered low/medium risk and two which are medium/high.

The Council SRR has appropriate detail for all risks, each of which have an inherent risk score, existing mitigations and controls, a residual risk score and further mitigations and controls to be put into place.

The Executive is responsible for considering overall financial and performance management and receives comprehensive reports on a quarterly basis. The Executive also receives reports relating to risk management and monitors the corporate risk register, as well as being responsible for key decisions and for initiating corrective action in relation to risk, performance and internal control issues. The risk management strategy and the SRR is regularly updated in consultation with Corporate Leadership Team (CLT) and presented to Audit Committee with the most recent report presented in September 2023. The SRR quarterly performance monitoring report is formally reviewed at CLT meetings, most recently in September 2023, with the meeting making detailed and substantial feedback comments on the document.

Due to the May 2023 local elections, there were no Audit Committee meetings between March 2023 and September 2023. The Council has Internal Audit arrangements in place with Internal Audit services provided by Audit West an external company who have provided the service to the Council for a number of years. The Head of Internal Audit's Annual report is presented to Audit Committee. The 2022/23 overall opinion regarding the Council's governance, risk management and internal control arrangements was that they were satisfactory (reasonable assurance) resulting in a moderate risk assessment.

Governance (continued)

Risk management and internal controls (cont.)

The Head of Internal Audit's Annual Report for 2022/23 noted that planned audit reviews (43 out of original plan of 48) had been completed, with just one report remaining in draft pending management response. The Internal Audit service, at the request of the Council Corporate Leadership Team (CLT) agreed to defer the remaining five audits into the 2023-24 plan. There were two audit reports issued where it was considered that the overall systems of internal control provided 'Limited Assurance', these related to Information and Communications Technology and Mandatory Training for Staff – both have been followed up with management to confirm that the recommendations have been implemented.

The Internal Audit service completed one detailed investigation in the 2022/23 year which related to allegations made against an employee. An in-depth review of the project management and decision-making process around the council's Garden Waste subscription service was also completed. 100% of recommendations due to be implemented in 2022-23 were followed-up by the Internal Audit service. Two recommendations made within audit reports were not agreed as management believed that there were sufficient mitigations which were agreed with Internal Audit.

Included in the 2022/23 Annual Governance Statement (AGS) were details of an internal audit report (submitted to Audit Committee in September 2023) which reviewed the arrangements relating Clevedon Seafront/ Hill Road Scheme and the review identified several issues, some of which if approached differently, would have contributed to better outcomes for this scheme. These included the budget for the project which evolved from originally being a relatively straightforward scheme with an estimated cost of £200,520, to a much bigger c£1.5m project and timings which were a constant challenge throughout the scheme. As such, there are learning points for the organisation in managing projects of this nature which should be considered in the future. The overall theme highlighting the need for closer monitoring (and early warning of risks) resulting from any deviation in spend from that anticipated within the original scheme design is included in the previous improvement recommendation on page 15.

In developing its 2022/23 AGS, the Council formally reviewed its corporate governance arrangements against its Local Code of Corporate Governance. Our work highlighted the effectiveness of the Councils governance framework including its system of internal control, this included review of minutes of Audit and Assurance Committee, Cabinet and Council to ensure that periodic monitoring and reviews are being reported appropriately and governance issues are addressed. This provided good assurance that there were no significant weaknesses in internal controls or governance arrangements during the 2022/23 year. This was corroborated by our 2022/23 financial statements audit and review of the 2022/23 AGS.

The Council seeks to engender an organisational culture that embraces the highest standards of conduct and accountability. Anti-fraud and corruption polices are kept under close review. The Council has a Whistleblowing policy to encourage individuals to raise issues of concern in a safe environment. The Council has not been subject to any material frauds in year.

The Council subscribes to Protect (formerly Public Concern at Work), who provide an independent confidential service where employees can report issues where they do not wish to use the internal processes.

The Council has established a Corporate Fraud team who investigate allegations of external fraud against the Council. Internal Audit investigate any employee fraud. The Council's counter fraud and anti-corruption arrangements are in accordance with the CIPFA Code of Practice on Managing the Risk of Fraud and Corruption 2014 .

Fraud awareness work took place during 2022/23, including through articles in the staff newsletter, online training and introduction of bespoke training videos and participation in the National Fraud Initiative. This awareness work helped lead to an attempted fraud of £58k being prevented. The Council's Counter Fraud Strategy, the Whistleblowing Policy, the Anti-Money Laundering Policy, and the Anti-Bribery and Corruption Policy were reviewed and updated during the year. We consider the Internal Control framework is satisfactory, based on internal audit opinions.

Informed decision making including the Audit Committee

The Council operates a Leader and Cabinet form of Executive. In addition, there are various scrutiny committees which hold the Cabinet to account. The work of the Council's committees is governed by the constitution. The constitution is regularly reviewed and updated, most recently in July 2023. The constitution is shared with all staff members on joining and is openly available on the Council's website. The Constitution sets out how the Council operates, how decisions are made and the policies and are followed to ensure that these are efficient, transparent and accountable to local people.

Our review of Executive, Full Council, Audit and Assurance Committee and other committee minutes indicates that key strategic decisions are subject to appropriate challenge and are supported by detailed papers. Senior officers are open to conversations during committee meetings. Senior officers attend to present their own area items and to respond to any questions. We have not seen evidence of discussions not being open. The Audit Committee provides appropriate challenge of financial and non-financial items. The members of the Committee have a good mix of experience and expertise and is supplemented by Independent Members to provide further challenge and expertise. The Committee is well attended with minimal absences.

Governance (continued)

Informed decision making including the Audit Committee (cont.)

The Council carries out a wide range of public consultation including consulting stakeholders on the draft budget for 2022/23. The communication and engagement plan included a dedicated webpage and media release; communication to members and staff; communication with Trade Unions; engagement with Area Management Teams; posts on the internet; intranet and use of social media.

Council business is conducted in public unless legislation deems it appropriate for it to be considered in private. Key decisions of officers are published on the Council's website. The Council has a Consultation Policy that sets out set out the Council's commitment to effective and efficient public consultation and sets the expectation that this commitment will be consistently applied, particularly in relation to the Council's key decisions. The Council consult with residents, businesses, partner bodies and other stakeholders and will use the results of the consultation to inform its decision-making processes, to develop and refine its policies, and to drive improvement in the services for which it is responsible.

The Council has appropriate performance in relation to overall AGS and Head of Internal audit opinion. The latest Ofsted opinion is supported by an agreed action plan which the Council is implementing. The Council's performance against a selection of key governance metrics for 2022/23 and 2021/22 is set out in the table 3 below.

Table 3- Council's performance against a selection of key governance metrics	2022/23	2021/22
Annual Governance Statement (control deficiencies)	Moderate	Moderate
Head of Internal Audit opinion	Satisfactory	Satisfactory
Ofsted inspection rating	Requires improvement to be good	Requires improvement

Governance (continued)

Standards and behaviours

The Council's constitution highlights how the Council will communicate the behaviours expected of staff and members. The AGS sets out that the Council has approved and adopted a code of corporate governance. The AGS is included in the annual review of the Constitution undertaken each year by the Assistant Director of Legal and Governance who is also the Council Monitoring Officer.

Review of the AGS and minutes of the Audit and Assurance Committee, Cabinet and Full Council meetings highlighted the effectiveness of the Councils governance framework including its system of internal control to ensure that periodic monitoring and reviews are being reported appropriately and governance issues are addressed. Review of Council meeting minutes and papers highlight there is evidence of leadership from senior officers and members in respect of meeting legislative/regulatory requirements and required standards of behaviour. We consider there to be an appropriate culture at all levels of the Council, review of committee minutes highlighted no significant breaches or issues have been raised with or reported to committees.

We consider the monitoring provides appropriate assurance that there were no significant weaknesses in internal controls or governance arrangements during the 2022/23 year. This was corroborated by our 2022/23 financial statements audit and review of the 2022/23 AGS.

The 2021- 2025 Procurement Strategy includes process to ensure it meets legislative and regulatory standards. The Council has adequate contract management and procurement procedures in place, and the council has dedicated procurement and contract management teams. There have been no significant issues reported in year with service provides or sub-contractors.

Conclusion

Overall, we found no evidence of significant weaknesses in the Council's governance arrangements for ensuring that it made informed decisions and properly managed its risks and we have concluded that appropriate arrangements are in place.

Improving economy, efficiency and effectiveness

We considered how the Council:

- uses financial and performance information to assess performance to identify areas for improvement
- evaluates the services it provides to assess performance and identify areas for improvement
- ensures it delivers its role within significant partnerships and engages with stakeholders it has identified, in order to assess whether it is meeting its objectives
- where it commissions or procures services assesses whether it is realising the expected benefits.

Assessing performance and identifying improvement

July 2023 Ofsted Inspection

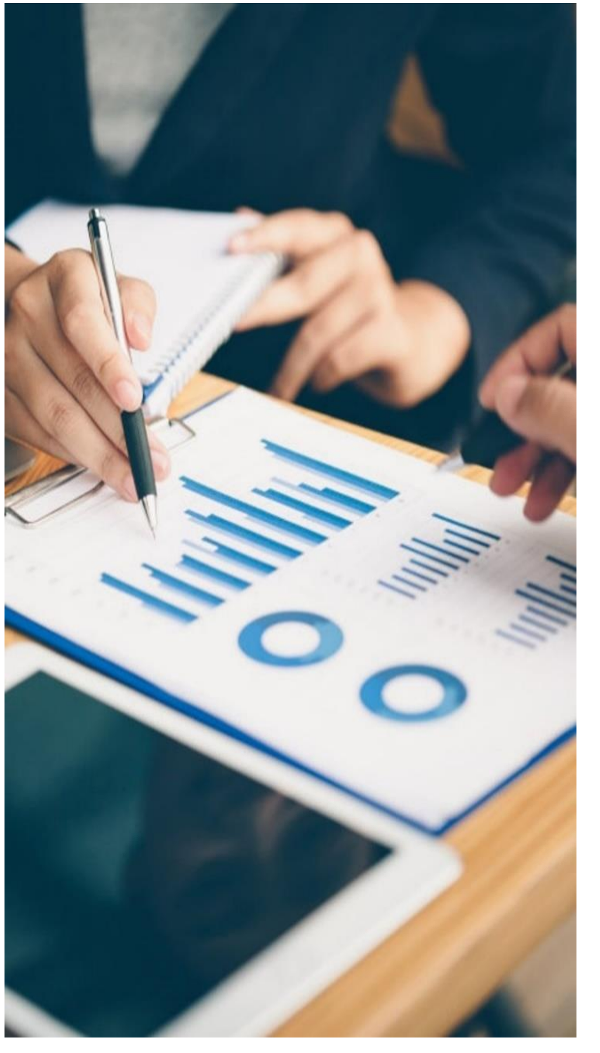
An Ofsted inspection of the Councils children's services (Inspection dates: 13 to 24 March 2023) reported: "Since the last inspection in March 2020, when the Council's children's services were judged to be requires improvement overall, the Council has not made sufficient progress and children and their families do not currently experience a consistently good service.

- The Covid-19 pandemic, restructure of the directorate, increasing need for services and a high rate of staff turnover within both the general workforce and the senior leadership team have all contributed to a pace of improvement that has been too slow for many children.
- Inspectors did not identify any children at risk of immediate harm. In some notable areas the impact on the lives of children and families in North Somerset has not been consistently good.
- Not all areas for improvement have been fully addressed since the last inspection and some positive changes to practice are not embedded. The quality of analysis and assessment of risk for children in need of help and protection and the effectiveness of management oversight and supervision remain areas in need of improvement. The exception is the quality of practice with care experienced young people who receive consistent support and services that meets their needs.
- Overall, inconsistencies in the quality of practice provided to children are too broad. The Council has a service-wide plan in place, aimed at securing the improvements needed with improved performance management and quality assurance systems in place."

The Council is in the process of updating the Council Children's Service Plan to ensure that all of the areas for improvement were fully addressed, and this was submitted to Ofsted in August 2023. The Council should continue the on-going oversight of the agreed Children's Service action plan undertaken by the Children and Young People's Services Policy and Scrutiny Panel. We have made an improvement recommendation regarding this detailed on page 23.

Assessing performance

The Council's performance against the Council Plan delivery schedule is reported on a quarterly basis to Executive. Performance against the Council Plan priorities is managed through progress made against quarterly deliverables and the outcomes of key performance indicators. It also brings together wider information, key facts and intelligence to explain how the Council is working and performing, including timelines and case studies to demonstrate the impact on residents and communities. With regards financial monitoring, we are satisfied sufficient detail is included to understand budget variances.



Improving economy, efficiency and effectiveness (continued)

Assessing performance and identifying improvement (continued)

Some slippage against these Council plan priority measures is to be expected given the on-going impacts of the COVID-19 pandemic throughout the 2022/23 financial year, it is important that performance continues to be monitored closely and there is a renewed focus on delivery of Council priorities.

The format of corporate performance reports will be reviewed as part of the arrangements supporting the new Council Plan.

The Local Government and Social Care Ombudsman (LGCSO) looks at complaints about councils where the complainant considers that the Council has not sufficiently addressed their concerns. The Annual letter from the LGCSO 2023 (July 2023) provided a breakdown of investigations that they have upheld to show the number of cases where the Ombudsman's recommendations have led to the Council resolving the issue. In the 2023 annual letter, the LGCSO included feedback that recommendations were not completed within the timescales agreed. Recommendations were made in six cases during the year. The LGCSO highlighted 55% of complaints investigated were upheld. This compares to an average of 72% in similar Councils. The six upheld decisions are based on a total of 11 investigations for the period between 1 April 2022 to 31 March 2023. The Council has undertaken appropriate actions for complaints made to LGCSO.

Benchmarking

Benchmarking was undertaken as part of our VfM work. We considered unit cost financial benchmarking comparing the Council to its statistical nearest neighbours. This identified Adult Social Care costs as high in comparison to benchmarked councils and within that three areas where the unit costs were very high:

- Learning Disability support – adults (18-64)
- Mental Health support – adults (18-64)
- Physical support – adults (18-64)

This is reflective of the overall challenges facing the provision of demand led services across all providers within the sector. There are a number of factors that the Council face which have contributed to these costs including:

- Costs associated with clients who transition from Children's Services into Adult Services with complex needs and spend in this area has outstripped other costs
- Packages of care have increased as a result of the backlog in elective care especially around those people who require joint replacement
- There is significant growth in inflation and also changes in demand demographics
- Increases in complexity of current clients. This includes issues such as people in care who develop dementia and an increase in cost does not mean more in recovered funds

There is also an element of benchmarking undertaken by the Council through the performance management process. Members are provided with detailed benchmark information through the performance update reports which includes a mixture of local and national targets. These are RAG rated to provide a predicted year end status and a direction of travel. The performance update reports identify areas for further improvement action and management actions in place to achieve this.

Council members are provided with suitable benchmarking information to provide assurance over performance and to allow challenge of any service that is not meeting expectations.

Partnership working

The Council's constitution sets out how it engages with stakeholders and partners through joint working arrangements, partnership boards and annual appointments to external organisations. The Council seeks resident views when developing proposals set out in Consultation and Engagement Strategy. The Council seeks feedback by carrying out an annual resident satisfaction survey.

The Council consulted stakeholders on their draft budget for 2022/23, this included online consultation as part of Council engagement. The Council undertook consultation regarding the Council Plan.

Improving economy, efficiency and effectiveness (continued)

Partnership working (cont.)

Within the Council Corporate Plan there is adequate evidence highlighting the Council's commitment to engage with residents. Part of this commitment is demonstrated through the formation of a North Somerset Citizens' Panel. The panel has recruited from people who live, work or study in North Somerset and has a current sample of over 550 people who want to actively be part of the council's vision and journey going forwards and are willing to participate in surveys, polls and focus groups. The panel offers an opportunity for early engagement with residents on the emerging themes within the MTFP and comments on specific areas within MTFP planning and /or future service delivery. The survey was open for a 2 - week period from 3 January to 12 January 2023 and 244 panel members submitted a response, some 40%, which compared to other stakeholder surveys we have seen is a relatively good level of response.

Commissioning and procurement

The Council has adequate contract management and procurement procedures in place, and the council has dedicated procurement and contract management teams. Our work identified there have been no significant issues reported in year with service provides or sub-contractors.

During 2022/23 appropriate Capital programme oversight was undertaken by the Executive. Officers are currently reviewing how much of the unspent balance will be required in future years and as a result this some budgets will be 'slipped' and included within next years' programme in line with delivery and completion of the schemes.

It is important that this review takes places because the capital programme is financed using a finite number of resources and so cannot simply absorb changes to costs that may be brought about by rising inflation. Project managers should provide assurance that any schemes that have experienced a delay of any kind can still be delivered within the approved budget envelope. The Council has put in place revised project management, risk management and capital governance arrangements over the last 12-18 months to provide greater oversight over such schemes.

Our improvement recommendation detailed on page 15 highlights the importance of effective monitoring of capital programme delivery.

Conclusion

Overall we are satisfied the Council has appropriate arrangements in place in its oversight of economy, efficiency and effectiveness. We have made one improvement recommendation relating to complaints resolution detailed on page 23.

Improvement recommendations

Improvement Recommendation 2	The Council should continue the on-going oversight of the action plan undertaken by the Children and Young People's Services Policy and Scrutiny Panel and subsequently to the Council Executive Committee.
Improvement opportunity identified	The Council need to pay close attention to this delivery of the action plan arising from recommendations in both Ofsted inspections; doing what it has agreed to do, on time, can help to rebuild complainants' trust and confidence after things have gone wrong.
Summary findings	Ofsted inspection of the Councils children's services (Inspection dates: 13 to 24 March 2023) highlighted – "Since the last inspection in March 2020, when the Council's children's services were judged to be requires improvement overall, the Council has not made sufficient progress and children and their families do not currently experience a consistently good service. The COVID-19 pandemic, restructure of the directorate, increasing need for services and a high rate of staff turnover within both the general workforce and the senior leadership team have all contributed to a pace of improvement that has been too slow for many children. Inspectors did not identify any children at risk of immediate harm. In some notable areas the impact on the lives of children and families in North Somerset has not been consistently good. Not all areas for improvement have been fully addressed since the last inspection and some positive changes to practice are not embedded. The quality of analysis and assessment of risk for children in need of help and protection and the effectiveness of management oversight and supervision remain areas in need of improvement. The exception is the quality of practice with care experienced young people who receive consistent support and services that meets their needs. Overall, inconsistencies in the quality of practice provided to children are too broad. The Council has a service-wide plan in place, aimed at securing the improvements needed with improved performance management and quality assurance systems in place." The Council is in the process of updating the Service Plan to ensure that all of the areas for improvement were fully addressed, and this was be submitted to Ofsted in August 2023.
Criteria impacted	Improving economy, efficiency and effectiveness
Auditor judgement	Our work has enabled us to identify a weakness in arrangements which we do not consider to be significant but have raised a recommendation to support management in making appropriate improvements. Progressing the actions management has identified to address the recommendations made will support the Council in addressing the improvements identified from our work. We consider that the timescales provided by management are appropriate and encourage the Audit Committee to monitor progress of implementation to gain assurance over the arrangements in place. The range of recommendations that external auditors can make is explained in Appendix B.
Management comments	It is the Council's view that the CYPS Policy and Scrutiny Panel is the appropriate forum for review and consideration of the Improvement plan. The most recent update from Ofsted in December 2022 was reviewed and considered at Council and all members are aware of progress. We have further reviewed the latest OfSted report and consider arrangements to be appropriate. We will continue to monitor effectiveness of our governance arrangements and this is recognised as a key issue in our Annual Governance Statement for 2022-23.

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Follow-up of previous recommendations

Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
The S25 statement should include supporting information on how the recommended minimum prudent level of General Fund balance is calculated	Improvement	August 2022	Management consider that there is sufficient information included within the S25 statement to allow members a full understanding on how the minimum prudent level of the General Fund balance has been reached. We have reviewed the report again in 2022-23 and consider that it is appropriate and allows member understanding	Yes	N/A
The Council should adopt a data quality policy	Improvement	August 2022	The Council has recently drafted a Data and Insight Strategy which has been adapted by ICTAB in the first instance and includes an action to develop and implement council-wide data quality standards.	Yes	N/A
The Council should consider including a sensitivity analysis to demonstrate the range of impacts that future funding reforms could have, even if they are not formally modelled in the MTFP. Sensitivity analysis should also be considered for other key financial planning assumptions. We also recommend that the MTFP covers the current year plus five, in accordance with CIPFA best practice	Improvement	August 2022	We have reviewed management's budget setting process and have noted that there is still a short fall in the provision of sensitivity analysis and scenario planning for 2022-23. We have continued our ongoing review of arrangements and have noted that scenario planning is included in the 2023-24 budget process and will review the robustness of the analysis in our review of arrangements in 2023-24	Yes	We will review the robustness of this analysis as part of the 2023-24 review of arrangements.

Follow-up of previous recommendations

Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
Treasury Strategy and Treasury Outturn reports should include detailed breakdowns of the budgets relating to interest costs, investment income and MRP, including performance against the budget at the year end. The Council should ensure it has sufficient risk mitigation strategies in place for commercial property and ensure compliance with the requirements of the revised Prudential Code	Improvement	August 2022	The Council have reviewed the annual investment report and consider that there is sufficient data within the report to allow the reader to understand the overall performance. Recognised in the 2020-21 AAR that the Council has financial risk mitigation measures in place for the existing commercial investments. The annual investment report also contains a range of financial information although, as management commented this could be enhanced.	Yes	N/A
The Corporate Risk Register should be reported to the Audit Committee on a more regular basis and risks should be mapped explicitly to corporate objectives.	Improvement	August 2022	The updated performance process has addressed the recommendation identified in 2020-21. Management consider that further information could be provided to members to give them full understanding of how risks have been arrived at	Yes	N/A
The Council should define its significant partnerships and develop a register that identifies the contribution that the partnerships makes to the Council's corporate objectives.	Improvement	August 2022	The Council has recognised that a partnership register would provide a single source of information and have added the recommendation into the work plan for the Partnership team.	WIP	N/A – action in place to implement already in place.
Where there is a significant difference between the in year estimated capital spend at a scheme level as part of the approved budget and the to date monitoring, we recommend a brief comment is included within the monitoring schedule to explain the reason for this.	Improvement	August 2022	We have reviewed the Capital reporting and consider that further information is required to allow the reader to understand what are the causes of any significant differences.	Partially	N/A – action to implement already in place

Follow-up of previous recommendations

Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
The Council should ensure it has effective governance arrangements in place in relation to North Somerset Environmental Services Limited (NSEC) to: • actively and routinely monitor the service and financial performance, so that NSEC is held to account and under performance is addressed • minimise the scope for conflicts of interest regarding the roles held by Council Officers on the NSEC Board.	Improvement	August 2022	The Council have reviewed and updated the governance arrangements for NSEC which has included the removal of any Council officer from the Board. It is the opinion of audit that there is still insufficient detailed performance information to allow members to understand any areas that require addressing and that contract terms are being met It was due to go to Council in May 2023 but deferred to July 2023 https://n-somerset.moderngov.co.uk/ieListDocuments.aspx?CId=169&MId=1059&Ver=4 in order to give new members time to gain a sufficient understanding on the waste governance	Yes	N/A
The Council's Executive should review performance against the corporate plan in public meetings and performance should be reviewed quarterly by the scrutiny committees in line with the Council's corporate performance framework.	Improvement	August 2022	Management considered that the arrangement in place were sufficient to address the requirements of performance management. The responsibility lies with scrutiny panels and quarterly performance updates are now published as part of the Executive Agendas https://n-somerset.moderngov.co.uk/documents/s4268/18%20Q2%20Performance%20Update.pdf	Yes	N/A
The Council should review and evaluate progress against its Children's Services Improvement Plan in a public committee meeting.	Improvement	August 2022	It is the Council's view that the CYPS Policy and Scrutiny Panel is the appropriate forum for review and consideration of the Improvement plan. The most recent update from Ofsted in December 2022 was reviewed and considered at Council and all members are aware of progress. We have further reviewed the latest OfSted report and consider arrangements to be appropriate	Yes	N/A

Follow-up of previous recommendations

Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
Management should review risk information presented to members and ensure sufficient information is provided.	Improvement	April 2023	The Council have updated our risk management strategy during 2022-23 and this was approved by the audit committee on 24 November 2022 https://n-somerset.moderngov.co.uk/documents/s4094/06%20Risk%20Management%20Strategy.pdf The strategy will be fully operational from 01 April 2023 and include nominated lead for each and five categories of risk. The Council consider that new strategy will cover this recommendation and do not intend to publish individual risk scores.	Yes	N/A
The Capital outturn programme showed that 48% of the programme had been spent in 2021-22 leading to a large slippage in the overall programme. Management should ensure that review of the overall budget is significantly robust and where there is a significant difference between the in year estimated capital spend, at a scheme level, as part of the approved budget, and the to date monitoring, we recommend a brief comment is included within the monitoring schedule to explain the reason for this and to ensure that large slippages are not incurred in future years.	Improvement	April 2023	The Council have taken steps to improve the governance arrangements and clarity of financial monitoring to members throughout 2022-23 and this process is now embedding and has been recognised by both the chairs of the audit committee and PCOM scrutiny. Significant variances in the capital budget are now reported in the Executive budget monitoring reports, including narrative. We recognise that the council is experiencing significant slippage in its capital programme, in common with many other local authorities, and steps are being taken to improve the allocation of budgets to align with deliverability.	WIP	IR re- made on page 15 of this report

Follow-up of previous recommendations

Recommendation	Type of recommendation	Date raised	Progress to date	Addressed?	Further action?
Scrutiny performance management is the responsibility of scrutiny panels to ensure that corporate strategies are being fully implemented. Management should consider whether the current level of scrutiny is sufficient to meet these requirements	Improvement	April 2023	The council has a finite amount of resources and must make decisions on how these are allocated to ensure that it can discharge all of its various statutory duties and has determined that sufficient resources have been allocated to ensure that an effective scrutiny function is in place, although recognises that this does not always provide for formal meetings to be held on a regimented quarterly basis. It should be noted that scrutiny activity is often considered within informal working groups and subject matter briefings and the council is assured that an overall level there is sufficient oversight of performance matters. Efforts will be made to review the timescales of meetings and ensure that the most relevant and up to date information is considered. This was deferred from May council as there had not been sufficient time to brief new members on waste governance in order to make the paper meaningful for Council. It is on the agenda for 11 July 23 and an all member briefing on 21st June.	Yes	N/A
Management should ensure that all capital projects are appropriately scoped and that full consideration is given to potential impacts on both the delivery timeframe and the overall costs of the project	Improvement	April 2023	The introduction of the Capital Programme Planning and Delivery Board (CPPD) from 2021/22 has brought about a series of improvements in terms of governance, oversight and monitoring associated with capital projects. This includes measures to review and track issues individual schemes as well oversight of the entire programme. Given the timescales associated with the creation of this Board it is not possible to retrospectively review the scope and funding for each project although has put in place measures to ensure that new projects are reviewed in detail prior to their approval. It has established a reporting framework to ensure that all projects are reviewed consistently throughout the year and also that issues are escalated and highlighted to the Board more frequently so that interventions and solutions can be discussed. The Board continues to update its underlying processes to ensure that it considers all types of risks and issues, this includes the recent change for project managers to understand and report on 'project creep' so that the Board can determine movements from the original scope. Whilst this area is still being fully embedded, significant change has already been delivered and improvements will continue to be made.	Yes	Further improvement recommendations relating to robust capital spend monitoring included in current AAR.

Opinion on the financial statements

Grant Thornton provides an independent opinion on whether the Council's financial statements:

- give a true and fair view of the financial position of the Council as at 31 March 2023 and of its expenditure and income for the year then ended, and
- have been properly prepared in accordance with the CIPFA/LASAAC Code of practice on local authority accounting in the United Kingdom 2022/23
- have been prepared in accordance with the requirements of the Local Audit and Accountability Act 2014.

We conducted our audit in accordance with:

- International Standards on Auditing (UK)
- the Code of Audit Practice (2020) published by the National Audit Office, and
- applicable law

We are independent of the Council in accordance with applicable ethical requirements, including the Financial Reporting Council's Ethical Standard.

Audit opinion on the financial statements

We issued an unqualified opinion on the Council's financial statements on 2 October 2023.

The full opinion is included in the Council's Annual Report for 2022/23, which can be obtained from the Council's website.

Further information on our audit of the financial statements is set out overleaf.

Opinion on the financial statements

Timescale for the audit of the financial statements

- The Audit Plan was presented to the Chair of the Audit Committee on 15 August 2023. The Audit plan was not presented to Audit Committee due to the elections and timing of meetings. Approval taken from meeting with Committee Chair and circulated to members
- The review of the accounts was undertaken between June and October 2023. This work was completed remotely
- The Council provided draft financial statements in line with the national timetable
- No significant issues were identified within the audit and good quality working papers were provided by management to support the audit process
- The opinion on the financial statements was issued on 2 October 2023, just missing the 30 September 2023 national timetable.

Whole of Government Accounts

To support the audit of the Whole of Government Accounts, we are required to examine and report on the consistency of the Council's consolidation schedules with their audited financial statements. This work includes performing specified procedures under group audit instructions issued by the National Audit Office.

Our work did not identify any issues.

Findings from the audit of the financial statements

- Management override of controls was reviewed through an analysis of the journal listing to select a sample based on the audit criteria for selecting high risk unusual journals. Review identified that both the value and volume of journals was significantly high which introduces inherent risk of both fraud and error. Our testing did not identify any issues within the journal sample
- Testing of assets with a nil NBV identified £24.7m of accumulated depreciation. We recommended that management review these assets to assess whether they remain operation or not.
- The IT audit undertaken in 2019-20 identified one significant control deficiency in relation to segregation of duties. Management have not yet addressed this issue, although believe that compensatory controls exist, and this directly impacted our journal methodology

More detailed findings are set out in our Audit Findings Report, which was presented to the Council's Audit Committee on 21 September 2023 with a final version issued on 2 October 2023. Requests for this Audit Findings Report should be directed to the Council.

Appendices

Appendix A: Responsibilities of the Council

Public bodies spending taxpayers' money are accountable for their stewardship of the resources entrusted to them. They should account properly for their use of resources and manage themselves well so that the public can be confident.

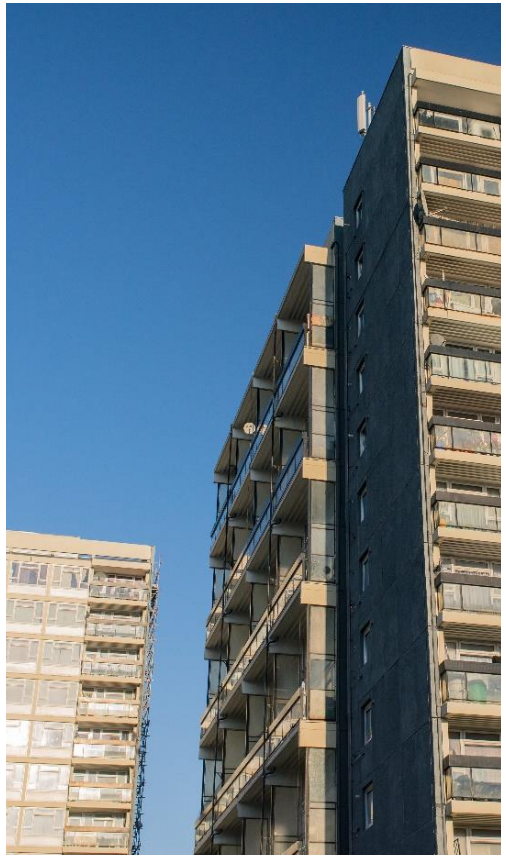
Financial statements are the main way in which local public bodies account for how they use their resources. Local public bodies are required to prepare and publish financial statements setting out their financial performance for the year. To do this, bodies need to maintain proper accounting records and ensure they have effective systems of internal control.

All local public bodies are responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness from their resources. This includes taking properly informed decisions and managing key operational and financial risks so that they can deliver their objectives and safeguard public money. Local public bodies report on their arrangements, and the effectiveness with which the arrangements are operating, as part of their annual governance statement.

The Chief Financial Officer (or equivalent) is responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the Chief Financial Officer (or equivalent) determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

The Chief Financial Officer (or equivalent) is required to prepare the financial statements in accordance with proper practices as set out in the CIPFA/LASAAC code of practice on local authority accounting in the United Kingdom. In preparing the financial statements, the Chief Financial Officer (or equivalent) is responsible for assessing the Council's ability to continue as a going concern and use the going concern basis of accounting unless there is an intention by government that the services provided by the Council will no longer be provided.

The Council is responsible for putting in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources, to ensure proper stewardship and governance, and to review regularly the adequacy and effectiveness of these arrangements.



Appendix B:
An explanatory note on recommendations

A range of different recommendations can be raised by the Council's auditors as follows:

Type of recommendation	Background	Raised within this report	Page reference(s)
Statutory	Written recommendations to the Council under Section 24 (Schedule 7) of the Local Audit and Accountability Act 2014.	No	N/A
Key	The NAO Code of Audit Practice requires that where auditors identify significant weaknesses as part of the Council's arrangements to secure value for money they should make recommendations setting out the actions that should be taken by the Council. We have defined these recommendations as 'key recommendations".	No	N/A
Improvement	These recommendations, if implemented, should improve the arrangements in place at the Council, but are not a result of identifying significant weaknesses in the Council's arrangements.	Yes	15 & 23

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North Somerset Council

Report to the Audit Committee

Date of Meeting: 25 January 2024

Subject of Report: Draft Treasury Management Strategy 2024/25

Town or Parish: ALL

Officer/Member Presenting: Mark Anderson, Principal Accountant (Resources & Financial Planning)

Key Decision: N/A
Reason: Not an Executive Decision

Recommendations
The Audit Committee is requested to;

i. note the contents of the report which summarise the key components of the draft Treasury Management Strategy for 2024/25 and associated impacts.

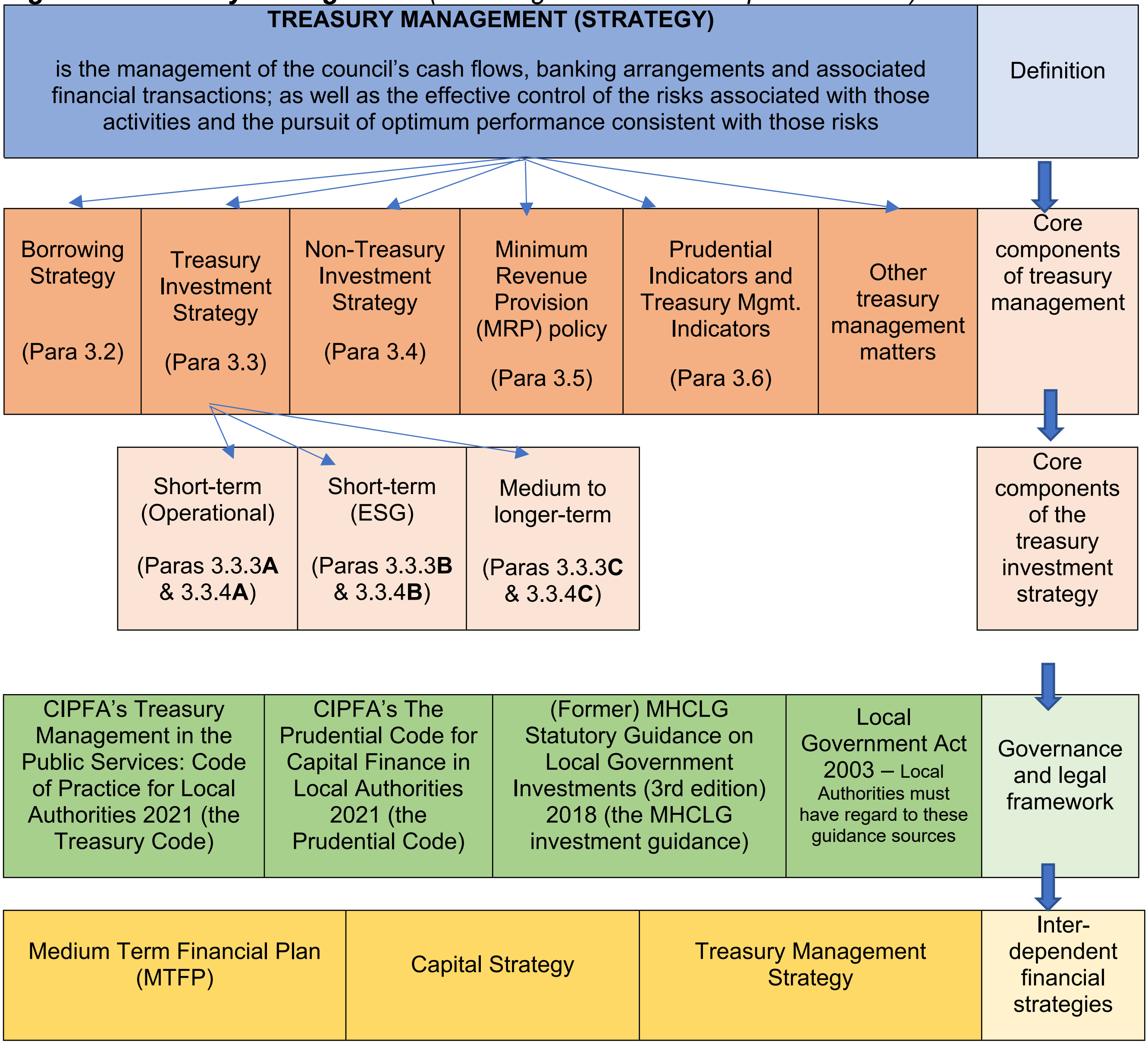
1. Summary of Report
The purpose of the report is to present the council's draft annual ***treasury management strategy*** (TMS) for the 2024/25 financial year and builds on the previous report on this matter, which was considered by the Audit Committee at its meeting in November 2023.

The report contains details of;
- how the council plans to manage its cash-flows and resources in the year ahead to ensure effective treasury management,
- the proposed Prudential & Treasury Indicators for 2024/25, and
- the proposed policy for making Minimum Revenue Provision in respect of the repayment of the council's external debt, within the revenue budget.

2. Policy
The council's budget process should ensure that all resources are planned, aligned, and managed effectively to achieve the corporate aims and objectives of the council. The council's treasury related strategies link directly into the revenue and capital budget planning processes and all aim to support effective service delivery across the council, in this year, as well as across the medium term.

Treasury management, its definition, constituent parts and its relationships with other policies and regulation is depicted in Figure 1 below.

Figure 1: Treasury Management *(including references to report structure)*



Each of the core components of treasury management, as noted above, are summarised in **Section 3** with further technical detail provided within the Treasury Management Strategy in **Appendix 1**.

3. Details

3.1 Introduction and background

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 therefore to ensure that this cash flow is adequately planned, with cash being available when it is needed. Much of the day-to-day **treasury** activity is linked to investing surplus monies in low-risk counterparties or instruments commensurate with the councils' low risk appetite, providing adequate liquidity initially before considering investment return.

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, subject to it being appropriate and affordable having considered premature redemption costs.

The contribution the **treasury management** function makes to the council is therefore 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.

As expected, given the nature of the transactions undertaken in this area, together with the significant amount and types of risk involved, treasury management is heavily regulated both in terms of legal statute, technical investment guidance provided by government departments as well as Codes of Practice issued by the Chartered Institute of Public Finance and Accountancy (CIPFA). The council is required to adhere to and give due regard, to all these relevant frameworks.

CIPFA defines treasury management as "the management of the local authority's borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks." This definition not only describes the various elements of treasury management activity, it also demonstrates how interlinked they are with other, which can make it difficult to explain the council's technical and strategic plans for the year ahead, in a way that can be easily understood.

The report has therefore been drafted to summarise the council's proposed approach for the 2024/25 financial within each of the following sections, with further detail contained within the appendices at the end of the paper.

- **Borrowing strategy** – paragraph 3.2
  To support the council's capital spending plans

- **Treasury investment** strategy – paragraph 3.3
  A) To support the daily operations of council services
  B) To ensure that the council is a responsible investor
  C) To manage longer-term cash-flows and generate financial returns to support the annual revenue budget

- **Non-treasury investment** strategy – paragraph 3.4
  To support place-making ambitions across the district and to support the annual revenue budget

- Minimum revenue provision policy – paragraph 3.5
- Prudential indicators and treasury management indicators 3.6

3.2 Borrowing Strategy

3.2.1. Background and local context:

In some instances, the council may find itself in a position whereby it may need to borrow short-term loans to cover unplanned cash flow shortages arising from operations. However, most of the council's borrowing activity is linked to its capital spending plans.

CIPFA's Prudential Code for Capital Finance in Local Government, requires the council to determine that all its capital expenditure and investment decisions are affordable, prudent, and sustainable, and it must ensure that it sets limits on the amount that it can afford to borrow in the context of wider capital planning.

To understand whether new borrowing plans can be deemed affordable, the council must first understand its current borrowing position and then overlay planned changes.

On 30th November 2023, the council held £164.6m of borrowing which it has drawn down over several years to fund previous capital expenditure.

- £129.4m of this debt is held with the Public Works Loan Board (PWLB) at an average rate of 4.00%
- £2.1m of this debt is held with Salix at an average rate of 0%
- £0.6m of this debt is held with local councils at an average rate of 4.04%
- £10.8m of this debt relates to debt managed by Bristol City Council, in respect of the former Avon County Council organisation
- £21.7m of this debt relates to long-term leasing arrangements, the largest of which relates to the Sovereign Centre

The prudential indicators associated with the council's long-term borrowing position (as noted in the report to Audit Committee in November 2023) show that existing loans are sustainable and affordable which is a reliable platform to move forward from.

The 2024/25 capital strategy is currently being developed although will not be complete in time for the Audit Committee report.

The TM report to the Executive in February will therefore include the actual level of new borrowing to support the capital plans, although this is not expected to be of a significant scale. The borrowing strategy noted below is therefore the most likely approach that the council will take although may be subject to slight change depending on the final capital strategy proposals.

3.2.2. Summary of current position:

The council currently holds £164.6m of long-term debt.

3.2.3. Objectives:

The council's main objectives when borrowing will be to achieve a low but certain cost of finance, while retaining flexibility should plans change in future.

3.2.4. Proposed Strategy for 2024/25:

Given the significant cuts to public expenditure and in particular to local government funding, the council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. Short-term interest rates are currently at a 15-year high but are expected to fall in the coming years and it is therefore likely that ‘external’ borrowing decisions will be deferred in respect of the 2024/25 financial year and the focus would instead be to draw-down and access the council’s internal borrowing through reducing cash balances.

During 2024 we will review all borrowings and debt facilities to ensure these continue to meet updated code requirements and deliver value for money for local taxpayers. The review will aim to ensure that we streamline our processes and decision making in order to maximise any contribution to the wider financial pressures faced by the council as well as to support the MTFP.

3.2.5. Borrowing strategy beyond 2024/25:

Given the levels of planned investment the council recognises that it may be required to borrow externally over the period 2025-2028 however, before any future borrowing is considered, officers would seek advice from the council’s treasury management advisors in relation to the potential costs of different options and to ensure an option proposal aligned to the objectives.

Whilst the council has previously raised most of its long-term borrowing from the PWLB it will consider long-term loans from other sources in the future, including banks, pension funds, and other local authorities, and will investigate the possibility of issuing bonds and similar instruments, to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code. An important point for local authorities to note is that they are no longer able to draw down loans from the PWLB if any of their capital spending plans relate to buying investment assets primarily for yield. Given that the council does not intend to borrow for yield, then it is likely that we will retain access to PWLB loans if needed.

3.3 Treasury investment strategy

3.3.1. Background and local context

Given that the primary purpose of treasury management is linked to the management of day-to-day cash-flows, then it must be accepted that the council will make investment decisions on an almost daily basis to smooth cash-flows and ensure that cash is planned and available when needed. These decisions and transactions are known as **treasury investments** and sums are often placed in short-term, low risk, highly liquid products which is commensurate with the council’s low-risk appetite.

In addition to the daily cash-flows that are related to the annual budget, at any one time the council’s balance sheet will show that it is also holding surplus cash-flows in respect of prior year activities, examples include the receipt of capital grants in advance of spending plans and the retention of monies within reserves, which may be held to fund future spending or be held to manage risk. It is necessary for these funds to also be placed in treasury investments during the year however, it is possible that some of these investments could be placed in a more strategic way that is more aligned to the nature and timescale of the relevant cash-flow, i.e., investments could be made across a longer-period of time if it is understood that the monies may not be required for a specific period of time.

Irrespective of whether the treasury related investment is placed for a short or a longer period, it is essential that **all** such investments are placed in accordance with the both the legal framework as well as the council’s approach to risk and defined objectives.

Before considering its Strategy for treasury investments for the year ahead it is therefore important to firstly understand the following, some of which are described in more detail throughout the report and the appendices;

- the current level of investment balances held and performance,
- current regulatory framework and future changes,
- annual cash-flow forecasts for the year ahead,
- planned profile of spending linked to capital receipts, grants, and reserves,
- new investment plans,
- market conditions, interest rates and future expectations,
- Environmental, Social and Governance (ESG) related considerations, and
- any other strategic decisions that may have been taken elsewhere within the council's treasury management strategy (i.e., borrowing strategy, approach to risk, required asset allocations, choice of assets).

3.3.2. Summary of current position:

In the past 12 months, the council's treasury investment balance has ranged between £162m and £213m which an increase over the levels in the previous 12 months. A review has been undertaken which show that this is, to a large extent, linked to legacy issues relating to Covid-19 and more recently the cost of living pressures, notably surrounding the cash flows related to the many support packages and intervention measures that the government continues to put place. The ability of the council to lever in external funding for large capital projects also reduces the need to draw down on the council's core cash-flows. Forecasts do indicate that these levels are expected to reduce by 31 March 2025 as sums are paid to businesses, providers and potentially returned to the government.

The majority of the council investments are held as short-term, with the duration being less than 1 year; £10m is held as long-term investments as the investments were placed several years ago for strategic purposes.

Arlingclose facilitate regular benchmarking programs to assess how the council's treasury management investment decisions and outcomes compare with other local authorities. Recent results show that the council's investment portfolio is not considered high risk, and, whilst investment returns have increased due to the current economic environment, the portfolio is providing returns in line with the risks being taken. This supports the council's approach in recent years whereby it has chosen to place funds prudently to protect monies and reduce exposure to risk.

Market conditions currently show that interest rates have likely reached their peak, which means that it will be important to consider the ongoing impact of interest rates on future treasury investment related decisions. The council's Medium Term Financial Plan assumes that £4.735m of additional income will be generated from higher returns during 2024/25. Of this, £0.835m will be reflected as a permanent increase in the investment income budget and £3.9m will be a temporary increase for 2024/25 only, to reflect the expected decrease in interest rates in future months.

The '*borrowing strategy*' described in para 3.2.4 above recommends that external borrowing is not taken, but spending will instead be offset against current surplus cash balances, i.e., it will be funded internally. This will mean that lower levels of surplus cash balances may be available during 2024/25.

3.3.3. Objectives: i.e., what we would like to happen

The council's **treasury investment** objectives for the year ahead cover the following areas;

A) Continued support of daily operational activity of the council as a whole to support business as usual activity ensuring compliance with current external regulation and internal guidance.

The council must ensure that its' treasury investments support the management of core cash-flows on a daily basis so that services can continue to be delivered to residents and this is achieved through the management of short-term cash deposit type investments.

There is currently a robust governance framework in place to cover these activities with approval levels and institutions clearly defined within the approved strategy and this is supported by routine reporting to the Audit Committee.

In terms of treasury related objectives, both the CIPFA Code and the MHCLG Guidance require councils to have underlying objectives supporting investment, with two of these being;

- Security – protecting the capital sum invested from loss; and
- Liquidity – ensuring the funds invested are available for expenditure when needed

The generation of yield is distinct from these two prudential objectives although guidance says that this <u>does not</u> mean that local authorities are recommended to ignore potential revenues but, recognises that it would be reasonable to consider what yield could be obtained, consistent with these priorities once proper levels of security and liquidity are determined, as well as the council's own appetite to risk.

B) For the council to pay regard to recent changes in investment guidance and to become a 'responsible investor' through the development of its treasury investment strategy which actively considers environmental, social and governance (ESG) principles when investing in the short-term. ESG policies involve central factors in measuring the sustainability and ethical impact of an investment within an organisation or sector.

ESG considerations are increasingly becoming an important factor in global investors' decision making, but the framework for evaluating investment opportunities is still developing and therefore the council's own approach to ESG investments is also currently limited and does not reflect ESG scoring or other real-time ESG criteria at an individual investment level.

It is proposed that the council supports progress in this area by approving a commitment to become a responsible investor and more specifically, that part of its short-term treasury investment activity (up to £6m) should be centred on delivering ESG outcomes.

C) Management of medium to longer-term investments – the council previously made a series of decisions following the identification of funds that were unlikely to be called upon in the short-term, to place these in a longer-term type investment.

The types of investments made, as well as the underlying objectives for these investments, often differ from the day-to-day short-term deposits. Whilst they still follow the CIPFA Code and the MHCLG Guidance in terms of security, the balance between liquidity and return become more blended. Previous decisions relating to these investments show that one of the core objectives was to bring a steady income stream into the councils' annual revenue budget. Whilst short-term interest rates can vary quite a lot over a relatively short period of time, some longer-term investments often provide a more stable annual return.

3.3.4. Treasury Investment Strategy for 2024/25: i.e., what we are planning to do to achieve the objectives for the year.

Given the breath of different objectives and requirements within the overall treasury function it is not possible to summarise the council's investment strategy within a single paragraph and so efforts have been made to summarise the different strands of the investment strategy across the following;

A) **Short-term investments** covering **daily operations** - the council will continue to place the majority of its short-term treasury investments in fixed and variable-term cash deposits with a range of counter-parties, which are often described as traditional investments.

B) Increase resilience by increasing the number of Money Market Fund counterparties.

This Strategy would ensure liquidity is maintained to support the council's daily operational activities, it limits the council's exposure to interest rate risk losses, reduces the risk of capital losses as well as minimising exposure to credit risk through diversification of counter-parties and countries. These will be achieved through the application of limits on the amount and period of its investments with individual counterparties, and in individual countries.

B) **Short-term investments** focused on **ESG** outcomes –the council will consider options for investments of up to £6 million of short-term funds with institutions who ring-fence the use of such funds for ESG-related matters.

The framework, scope, governance, and investment criteria has been developed through consultation with the Audit Committee and treasury advisers over the past 12 months.

It is anticipated that any new investments will give due regard to the current credit ratings for security as they would need to remain in line with the wider council policy however, where appropriate and at the council's discretion, some flexibility will be provided to allow for slightly longer durations of investment and potentially lower returns to support the ESG focus.

When investing in banks and funds, the council would seek to 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.

C) **Longer term investments** - the council will continue to monitor and assess the performance of its existing medium to longer-term investments to ensure that they continue to meet the required core objectives, which are largely in alternative investment products although has **no plans** to place any more funds in long-term investments during 2024/25.

This is largely because of the work that has been done to review the medium-term capital financing requirements of the council, linked to borrowing plans, which shows that a large proportion of medium-term funds will be required and would therefore not be available to be locked away.

This Strategy continues to recognise that the current level of longer-term cash balances are appropriately balanced over the period, and that these investments provide some diversification of the portfolio in terms of product, counter-party / credit risk, and inflationary risk. Over recent years it has been seen that in a low interest rate environment these types of investment will often provide higher rates of return compared to traditional investments however, it must be accepted that they may also potentially provide a capital loss should prices fall beyond the initial investment levels. Any capital loss generated would need to be reflected within the council's annual revenue budget from April 2025, which is when the extended statutory override period expires.

3.3.5. Approved counterparties and limits:

The council may undertake treasury related investments of surplus funds with any of the counterparty types below, subject to the limits shown.

Table 3: Approved counterparties and limits

Sector	Overall Limit[1]	In-house Limit	Tradition Limit	Time Limit	Sector Limit
UK Central Government	**no limit**	unlimited	unlimited	50 years	no limit
UK Local Authorities[3]	**£15m**	£10m	£5m	25 years	no limit
Banks* and other organisations* (unsecured) whose lowest published long-term credit rating from Fitch, Moody's and Standard and Poor's is:					
AAA	**£30m**	£30m	£0m	5 years	no limit
AA+	**£25m**	£25m	£0m	5 years	no limit
AA	**£22m**	£22m	£0m	4 years	no limit
AA-	**£20m**	£16m	£4m	3 years	no limit
A+	**£18m**	£14m	£4m	2 years	no limit
A	**£16m**	£12m	£4m	13 months	no limit
A-	**£13m**	£9m	£4m	13 months	no limit
UK Building societies (unsecured) that have an asset size of more than £0.4bn*	**£10m**	£6m	£4m	13 months	£50m
Money market funds[2] and similar pooled vehicles whose lowest published credit rating is AAA*	**£15m**	£15m	£0m	N/A	no limit
Pooled Investment funds	**£5m per fund**	*£5m per fund*	£0m	N/A	£10m
ESG-focussed short term deposits	**£6m**	£6m	£0m	13 months	no limit
The Council's Bank accounts	**net £9m**	net £9m	£0m	no limit	no limit

[1] limits shown are per organisation.
[2] as defined in the Local Authorities (Capital Finance and Accounting) Regulations 2003
[3] as defined in the Local Government Act 2003
**There is no intention to restrict investments to banks and building society deposits, and investments may be made with any public or private sector organisation that meets the credit rating criteria above.*

This table must be read in conjunction with the notes and details in **Appendix 1**

3.3.6. Investment limits:

The maximum that could be lent to any one organisation (other than the UK Government) will therefore **be £30m**. This will limit the potential loss in the case of a single financial institution. It should be noted that a group of banks under the same ownership will be treated as a single organisation for limit purposes.

3.3.7. 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 considered.

3.4 Non-treasury investment strategy

Non-treasury investments often include purchases which are deemed to be capital expenditure in nature, whether that be the purchase of financial assets, such as share capital in any body corporate or non-financial assets, such as the purchase of land or buildings.

To date, the council has not purchased share capital as this would provide potential exposure and further risk in terms of capital losses, which goes against the legal and regulatory framework in place for treasury related investments.

The council does however have non-treasury investments in the form of property through the commercial investment portfolio. The commercial strategy was approved by Council in January 2019, following professional advice provided by Montagu Evans. The strategy established a framework under which the council could acquire a portfolio of investments in commercial property which generate an income stream which can be used to contribute to the revenue budget pressures, whilst potentially providing capital appreciation over the longer-term.

Under this arrangement two assets have been acquired and the arrangements for the governance and management of associated risks of the council's service investments and commercial property investments is detailed in Section 5 of the Treasury Management Strategy shown at **Appendix 1**.

No further commercial investments are being sought as this would be prohibited under the new borrowing permissions, which do not allow councils to borrow to generate a yield. There are no proposed changes to this area of the strategy for 2024/25.

3.5 Minimum Revenue Provision Statement

When the council funds capital expenditure by long-term borrowing, the costs are charged to the council tax-payer in future years, reflecting the long-term use of the assets procured. There are two elements to this cost – the interest on borrowing is charged in the year it is payable, and the principal (or capital) element is charged as a "minimum revenue provision" (MRP).

The Local Government Act 2003 requires the council to have regard to the former Ministry for Housing, Communities and Local Government's guidance on Minimum Revenue Provision (the MHCLG Guidance), most recently issued in 2018.

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.

The MHCLG Guidance requires the council to approve an Annual MRP Statement each year and recommends several options for calculating a prudent amount of MRP. The council's policy adopts options recommended in the Guidance, as well as locally determined prudent judgements in applying the recommended methodologies.

It is recommended that the council continues to apply the following policy to determine its MRP for 2024/25:

a. For capital expenditure incurred before 1st April 2008, the MRP for 'Supported borrowing' will be determined by writing down the Council's Capital Financing Requirement using a 'straight line' basis over the estimated average life of the relevant assets of 33 years. This approach results in the council charging the same value each year for this element of the MRP.

b. For capital expenditure incurred after 31st March 2008, the MRP for 'Prudential borrowing' will be determined by charging the expenditure over the expected useful life of the relevant asset, starting in the year after the asset becomes operational.

c. For assets acquired by finance leases, and for the transferred debt from Avon County Council, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability.

d. Where former operating leases have been brought onto the balance sheet on 1st April 2024 due to the adoption of the IFRS 16 Leases accounting standard, and the asset values have been adjusted for accruals, prepayments, premiums and/or discounts, then the annual MRP charges will be adjusted so that the total charge to revenue remains unaffected by the new standard.

e. Capital expenditure incurred during 2024/25 will not be subject to an MRP charge until 2025/26.

The 2024/25 capital strategy is being developed but will not be complete in time for this report. The TM report to the Executive in February will therefore include confirmation that MRP associated with the capital spending approvals has been included within the budget for 2024/25 and the planned spending for 2024/25 has been factored into the council's medium term financial plan for 2024/25.

Temporary arrangements are currently in place to recognise that the council had previously set aside more than the required minimum provision, and temporarily reduces the MRP chargeable on pre-2008 expenditure over eight years in order to regularise the position. This temporary arrangement comes to an end next year which will result in the MRP on pre-2008 expenditure increasing to the full 33-year rate. There is a growth bid in the MTFP, and capital financing impacts are featured in this report as well as the MTFP report.

3.6 Prudential Indicators

Under the Local Government Act 2003, and the associated CIPFA Prudential Code for Capital Finance in Local Authorities, 'Prudential Indicators' relating to the revenue implications of capital programme decisions need to be approved by members and considered when setting the revenue and capital budgets.

The 2024/25 capital strategy is being developed but will not be complete in time for this report. The TM report to the Executive in February will therefore include the prudential indicators although the Treasury Management and investment indicators are included in this report, at **Appendix 2.**

The CIPFA Treasury Management Code of Practice also requires locally decided indicators relating to treasury activities to be approved. These indicators provide information to Members on the affordability of the council's borrowing plans, and whether the impact of treasury management actions on the council's revenue budget are sustainable. The indicators are detailed in **Appendix 2**.

4. Consultation

The Audit Committee has a key role to play in reviewing the council's treasury management arrangements and practices, and they routinely receive performance monitoring reports on the subject covering both prior and current years, as well as reports which provide an opportunity for discussion to take place to consider the proposed strategy for the year ahead. The latest reports were considered by the Committee in November 2023 and a further report will be considered at the meeting in January 2024.

Over recent years Member training and workshops have been provided to support understanding of technical matters, with the latest session held being in December 2023. The timing of the session enabled further opportunities to consider the proposed Strategy for 2024/25.

Previous briefings were facilitated by Arlingclose, the council's external advisors and featured information relating to the legal framework, the definitions and differences between capital and treasury investments and impacts, the types of investments available to the council and how these might fit in with the council's borrowing plans, as well as further information to understand the more strategic factors which are likely to influence treasury strategy decisions of a council. It is proposed that they also attend future briefings.

5. Financial Implications

Financial implications are contained throughout the report. Treasury management decisions impact on both the revenue budget and the balance sheet in current and future years. However, an additional summary has been included to provide a high-level overview of the key components linked with capital financing and investment decisions.

	2023/24 Forecast £000	**2024/25 Estimate £000**
Interest payable on borrowing	6,015	6,015
Interest receivable on investments	-6,797	-6,286
Minimum revenue provision	6,572	8,608
Total	**5,790**	**8,337**
MRP analysis; - Supported Borrowing Minimum Revenue Provision - Prudential Borrowing Minimum Revenue Provision	 900 4,855	 1,220 6,575

- Ex-Avon Loan Debt Minimum Revenue Provision	452	433
- Finance Leases Minimum Revenue Provision	365	380

6. Legal Powers and Implications

Under the Local Government Act 2003 s1, and s12, local authorities may:

- invest money or borrow money:
- for any purpose relevant to their functions
- for prudent financial management

Under Local Government Act 2003 s2, and s13, local authorities must not:

- exceed their affordable borrowing limit
- borrow in foreign currency
- mortgage their property as security for loans borrowed

Under Local Government Act 2003 s3, s14, and s15, local authorities must:

- set and review affordable borrowing limits / authorised limits
- have regard to guidance published by CLG and CIPFA
    - CLG Investment Guidance
    - CIPFA Code of Practice on Treasury Management
    - CIPFA Prudential Code

The council has adopted 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 it to approve a treasury management strategy before the start of each financial year.

Under this guidance, the role of the (Full) Council is to:

- Set the budget and capital programme, including debt and investment interest, and the Minimum Revenue Provision
- Approve the Capital Strategy
- Approve the Treasury Management Strategy (which includes the (Non-Treasury) Investment Strategy)
- Approve the Prudential Indicators
- Approve Treasury Management Indicators
- Approve the MRP policy statement

Under the Local Authorities (Functions and Responsibilities) (England) Regulations 2000, local authorities must not delegate the approval of an annual strategy to any committee or person.

The role of the Executive is to consider these strategies, and, if appropriate, recommend them for approval by Council.

Treasury risk management at the council 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 Council to approve a treasury management strategy before the start of each financial year. This report fulfils the council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

7. Climate Change and Environmental Implications

Over recent years the council has made concerted efforts to better understand the extent to which its overarching treasury management strategy has or may have on climate change and other environmental implications. This has been a challenge because many of the decisions relating to either borrowing or investments will have few direct impacts although there could be many indirect impacts though the ongoing actions or decisions of other organisations.

For example, when the council places a short-term fixed cash deposit type investment with either a bank, building society or another local authority, then its contractual arrangement is linked to the terms of that trade deal (e.g., value, maturity date, interest rate etc). The details relate to the temporary exchange of the cash sum and there are no other restrictions about what will happen with money. The counter-party 'could' then choose to invest it into something that is not supported by the council.

Until recently the council recognises that it has had limited choice or options in this area however, some degree of change is expected to happen following the emergence of Environmental, Social and Governance (ESG) policies. This is where organisations are choosing to bring other considerations into their treasury strategies and decision-making processes and also introduce new investment products or services to the market.

The council welcomes the introduction of ESG policies and hopes that they will provide a broader range of opportunities that can be considered within future investment decisions, particularly those that will deliver positive outcomes for climate change and the environment more generally.

The ESG investment policy is set out in **Appendix 4** and will not detract from the core functions that need to take place within the existing treasury management strategy, i.e., the management of cash-flows and also meeting the requirements within the approved revenue budget, but it will provide an opportunity to ensure that climate and other environmental implications are considered and reported on.

The council's ESG investment policy must still be compliant with the external and internal regulatory framework and would therefore continue to give focus to security and liquidity, then yield.

8. Risk Management

Members will be aware that there is a direct link between the levels of risk and the levels of return achieved on investment, although there are many other factors which also affect the capital financing budgets.

The council's treasury management activities expose it to a variety of financial risks, notably:

a. credit risk – the risk that other parties might fail to pay amounts due to the council. Includes bail-in risk – the risk that shareholders and depositors in banks and building societies bear losses in the event of counter-party's failure or reduction in net asset value,
b. liquidity and re-financing risk – the risk that the council might not have funds available to meet its commitments to make payments as they fall due,
c. market risk (interest rate and price risks) – the risk that financial loss might arise for the council because of changes in such measures as interest rates, investment valuations, and stock market movements.

The council's Treasury Management Strategy sets out the council's approach to managing these risks.

A summary of the risks relating to treasury management that the council is exposed to, and the mitigation arrangements in place through the Treasury Management Strategy, is detailed at **Appendix 3.**

The priority of the Treasury Management Strategy will continue to be the reduction of risk to safeguard public resources.

The risk appetite of the council is low to give priority to the security of its investments. The council will also aim to achieve the optimum return on its investments commensurate with desired levels of security and liquidity.

It should be noted that the council's Treasury Management Strategy sets out how the council manages and mitigates these risks but cannot eliminate risks completely.

9. Equality Implications

Have you undertaken an Equality Impact Assessment? N/A

10. Corporate Implications

The safeguarding of public money is critical to the council's reputation, and the measures contained within the report are intended to address member and public concerns and ensure an appropriate balance of return on investment whilst ensuring managing associated risks.

11. Options Considered

This report has been developed alongside the Medium Term Financial Plan and revenue budget and the Capital Strategy, which supports the capital programme, which means that decisions are fully integrated. It also sets out the council's expectation for interest rates and highlights the uncertainties and risks in the forecast due to market conditions.

The report considers those aspects of treasury policy that change annually or more frequently, highlighting the council's views or interpretation of factors that may influence treasury management decisions and proposes how these matters will be dealt with during 2024/25.

The CIPFA Code and MHCLG statutory guidance require the authority to set out its approach to non-treasury investments. A summary of the impact and the council's approach is included in **paragraph 3.4** of this report.

The council's Treasury Management Strategy is broadly consistent with the previous strategy and is developed from and complies with the council's Treasury Management Policy and takes account of the CIPFA code and MHCLG guidance referred to above. That being said, a new recommendation has been included with regards to making a commitment to become a responsible investor in the future.

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Appendices:

1. Treasury Management Strategy for 2024/25
2. Prudential Indicators for 2024/25
3. Treasury Risk Register
4. ESG investments policy
5. Glossary of Terms
6. Arlingclose Economic & Interest Rate Forecast – December 2023

Background Papers:

Treasury Management Strategy 2023/24

Other relevant guidance includes:
- CIPFA – The Prudential Code for Capital Finance in Local Authorities 2021
- MHCLG – Statutory Guidance on Local Government Investments (3rd edition) 2018
- CIPFA - Treasury Management in Public Services – Guidance notes for local authorities 2021

1 EXECUTIVE SUMMARY

Treasury management is the management of the council's cash flows, borrowing and investments, and the associated risks. The council has and will continue, to borrow and invest substantial sums of money and is therefore exposed to wide range of risks which could have material consequences, such as the loss of invested funds. The successful identification, monitoring, and control measures in respect of financial risk are therefore central to the council's prudent financial management and operation within this area.

The council maintains an overarching treasury management 'strategy' which is supported by a range of individual policies which aim to describe some of the principles and practices to which the different areas of treasury related activity will comply.

It is important to note that this document contains a lot of detailed and sometimes technical information that will outline the risks and issues pertaining to the management of the council's cash-flows and ultimately inform any decisions that may be taken as a result.

Decisions that relate to this area are clearly significant however they are not undertaken in isolation but instead are driven by many factors and considerations, whether those be external influences (such as guidance, regulation, or market forces) as well as internal influences (such as other financial and operational strategies, council priorities or the approach to risk).

Given that an overarching strategy cannot document or describe all of those issues in detail, this document is not intended to be a prescriptive listing of all of the council's considerations or processes, the document will instead provide sufficient information to outline the council's approach and framework in core areas.

Alongside this policy, the council must have regard to the (former) Ministry for Communities and Local Government (MHCLG) guidance (the MHCLG guidance), under section 15(1)(a) of the Local Government Act 2003. This guidance provides for each authority to determine its own controls within a given framework.

Any external investment managers employed by the council are required, contractually, to comply with this Strategy.

Given that the underlying regulatory framework supporting treasury management activities remains broadly unchanged from 2023/24, as have the council's Corporate Plan aims and objectives, it is not proposed to make significant changes to the Strategy for 2024/25 financial year.

One area of change will however be the council's decision to become known as a responsible investor and the inclusion of an ESG focused investment policy in **Appendix 4**. Further details and supporting information are contained throughout the report and the strategy document.

2 STRATEGY OVERVIEW

Under the Local Government Act 2003, the council may invest money or borrow money:
- for any purpose relevant to its functions, and
- for prudent financial management.

The council could potentially invest its money for three broad purposes:
- Treasury management investments – i.e., management of operational cashflows. Investment of surplus cash balances generated as a result of its day-to-day activities, for example when income is received in advance of expenditure,
- Service investments - to support local public services by lending to, or buying shares in other organisations, and
- Non treasury related investments - to earn investment income, usually rental income, and to provide capital appreciation, from a portfolio of property investments.

The Strategy for 2024/25 in respect of the following aspects of the treasury management function is based upon the S151 Officers views on risks and interest rates, supplemented with advice provided by the council's treasury advisors, currently Arlingclose Ltd.

The strategy covers:
- Section 3 - current treasury portfolio
- Section 4 - the treasury investment strategy
- Section 5 - the non-treasury investment strategy
- Section 6 - the borrowing strategy
- Section 7 - interest rates and economic outlook
- Section 8 - other treasury management matters

3 CURRENT TREASURY PORTFOLIO

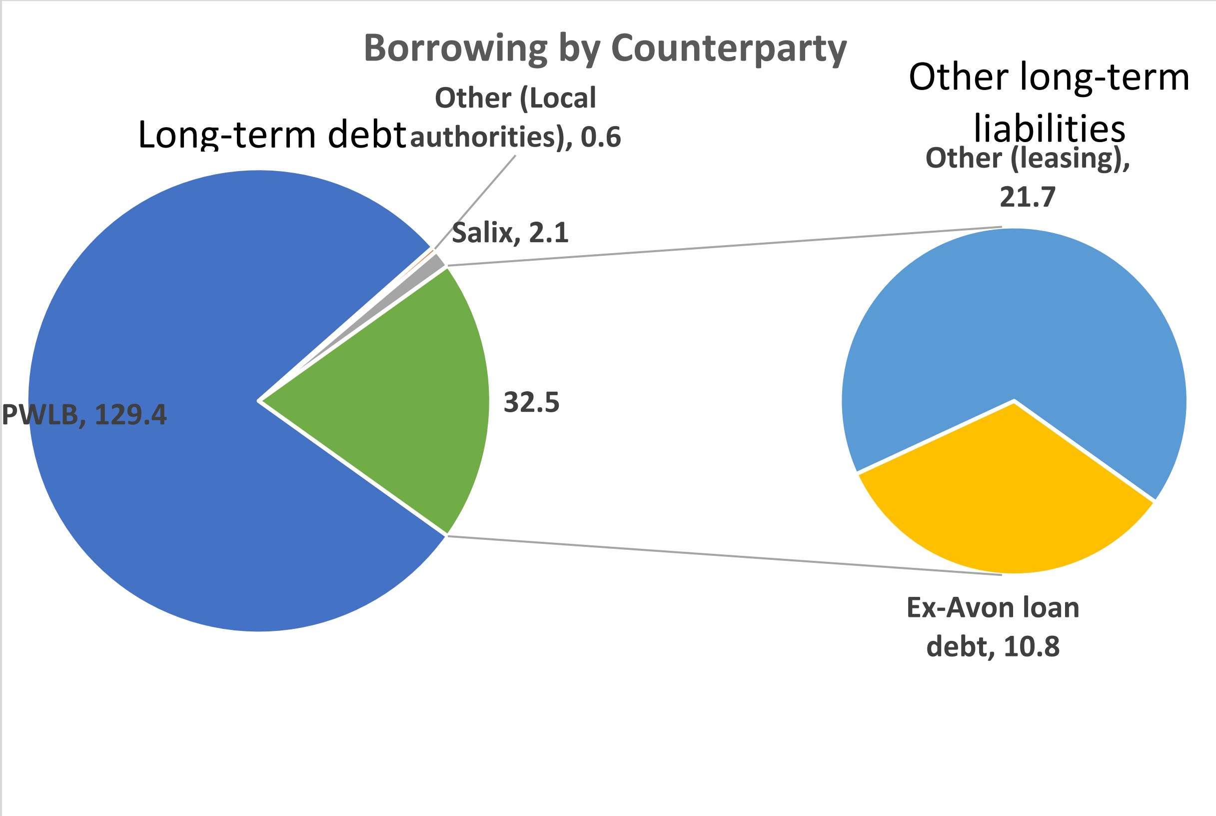
The Council's current treasury portfolio, as at 30th November 2023 is as follows:

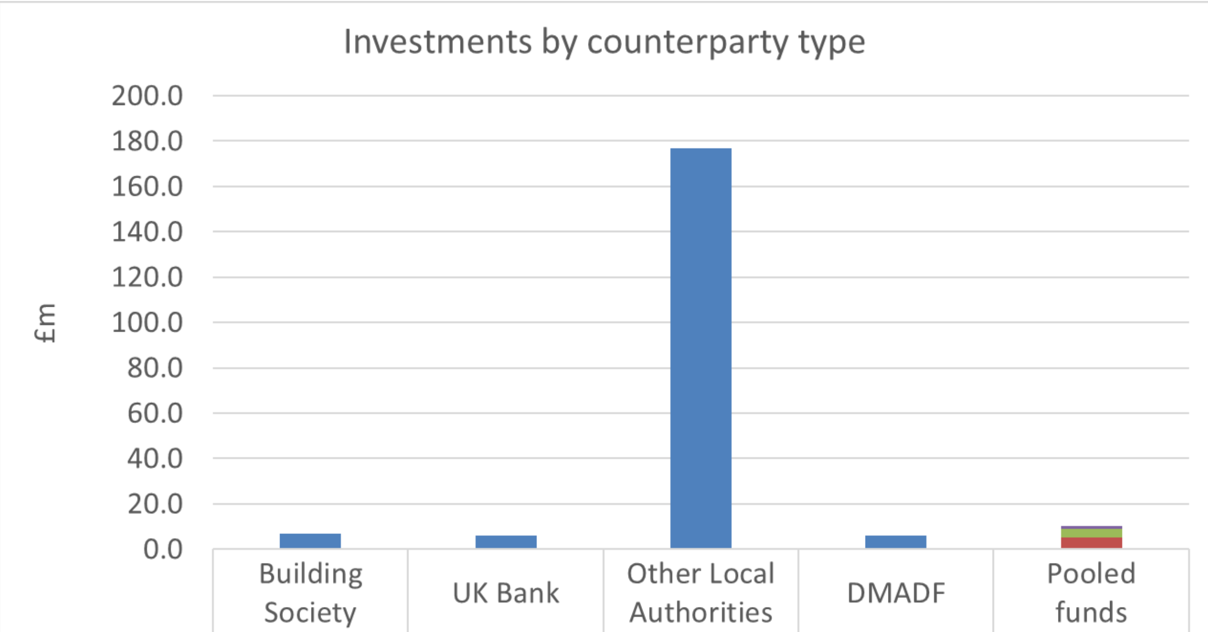
Table 4: Current portfolio of borrowing and investment balances

LONG-TERM DEBT	**Principal £m**		**Average rate**	**Average term**
Fixed rate – Public Works Loans Board Salix - Other (Local authorities)	£129.4 £2.0 £0.6	 £132.0	4.00% 0.00% 4.04%	1-36 years 1-5 years Notice
Other long-term liabilities; - Ex-Avon loan debt - Other (leasing) *	 £10.8 £21.7	 £32.5	 4.75% 4.60%	 1-30 years 1-40 years
TOTAL DEBT		**£164.5m**		
SHORT-TERM TREASURY INVESTMENTS	**Principal £m**		**Average rate**	**Average term**
Managed in-house; - UK banks - Local authority/ DMO	 £6.0 £180.0	 £186.0	 5.09% 4.85%	 12 months 10 months
Cash managed by Tradition; - Local authority - Building Society	 £3.0 £7.0	 £10.0	 4.13%	 12 months
LONG-TERM TREASURY INVESTMENTS	**Principal £m**		**Average rate**	**Average term**
Managed in-house; - CCLA - UBS Multi Asset Income Fund - Ninety-One Diversified Income Fund	 £5.0 £1.0 £4.0	 £10.0	 4.90% 4.90% 3.88%	 3-5 years 3-5 years 3-5 years
TOTAL TREASURY INVESTMENTS		**£206.0m**		
TOTAL NET INVESTMENT		**£41.5m**		

**The lease principal, rate, and term as at the previous year end (31st March 2023) - updated figures will be calculated at the end of the financial year.*

Chart 4: Current portfolio of borrowing and investment balances





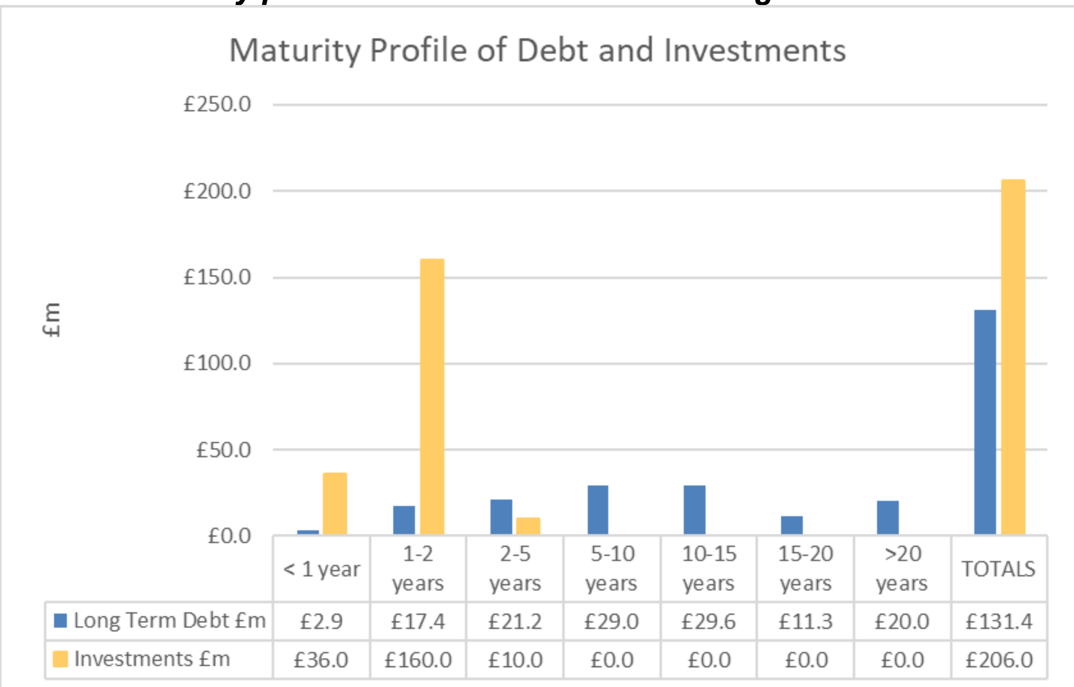
	Building Society	UK Bank	Other Local Authorities	DMADF	Pooled funds
UBS					1.0
NinetyOne					4.0
CCLA					5.0
Total	7.0	6.0	177.0	6.0	

The maturity profile of the Council's PWLB borrowing, and investments is as follows (excluding Avon loan debt and lease liabilities):

Table 5: Maturity profile of the Council's PWLB borrowing and investments

MATURITY PROFILE	PWLB LONG TERM DEBT £m	INVESTMENTS £m	NET DEBT / (INVESTMENT) £m
Maturing Jan to March 2024	£2.9	£36.0	(£33.1)
Maturing 2024/25 & 2025/26	£17.4	£160.0	(£142.6)
Maturing 2026/27 to 2028/29	£21.2	£10.0	£11.2
Maturing 2029/30 to 2033/34	£29.0	£0	£29.0
Maturing 2034/35 to 2038/39	£29.6	£0	£29.6
Maturing 2039/40 to 2043/44	£11.3	£0	£11.3
Maturing after 2043/44	£20.0	£0	£20.0
TOTALS	**£131.4**	**£206.0**	**(£74.6)**

Chart 5: Maturity profile of the Council's borrowing and investments



4 TREASURY INVESTMENT STRATEGY

4.7 The council typically receives its income in cash (e.g., from taxes and grants) before it pays for its expenditure in cash (e.g., through payroll and invoices). It also holds reserves for future expenditure and collects local taxes on behalf of other local bodies and central government. These activities, plus the timing of borrowing decisions, lead to a cash surplus which is invested in accordance with guidance from CIPFA.

4.8 **Objectives:** Both the CIPFA Code and the MHCLG Guidance require councils to invest their 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 council aims to be a responsible investor and will consider environmental, social and governance (ESG) issues when investing.

4.9 **Strategy:** The council 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.

4.10 The CIPFA Code does not permit local authorities to both borrow and invest long-term for cash flow management. But the council 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.

4.11 The council's current investment strategy allows surplus cash balances to be managed by two treasury teams, each having distinct and separate controls and flexibilities. This allows the council to spread risk by investing in different financial products, and utilising experienced external cash managers, who do not have responsibilities for managing the council's daily cash-flows. The treasury teams are;

a. Tradition UK Ltd
b. In-house Treasury Team

4.12 **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 council's ESG policy does not currently include ESG scoring or other real-time ESG criteria at an individual investment level.

4.13 The council has developed a framework for ESG related investments through consultation with the Section 151 Officer, members of the Audit Committee and also the council's treasury management advisors Arlingclose. It is anticipated that the credit rating of security of such deposits would need to remain in line with the wider council policy however, where appropriate and at the council's discretion, some flexibility will be provided to allow for slightly longer durations of investment and potentially lower returns to support the ESG focus.

4.14 When investing in banks and funds, the council 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.

4.15 The ESG investment policy will not detract from the core functions that need to take place within the existing treasury management strategy, i.e., the management of cash-flows and meeting the requirements within the approved revenue budget. The policy ensures that climate and other environmental implications are considered and reported on. The ESG Investment Policy is included in **Appendix 4.**

4.16 **Business models:** Under the IFRS 9 standard, the accounting for certain investments depends on the council's "business model" for managing them. The council 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.

4.17 **Approved counterparties:** The approved counterparties and notes are included in **Table 3** in the main body of the report. Further details on each of the permitted counterparties are included below.

4.18 The maximum duration of the investment will depend upon its lowest published long-term credit rating, time limits are included within the table.

4.19 Long-term investments will be limited to 50% of the counter-party limit (except the UK Government). The combined value of short-term and long-term investments with any organisation will not exceed the limits for investments in the table above.

4.20 **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.

4.21 **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.

4.22 **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 council will take care to diversify its liquid investments over a variety of providers to ensure access to cash at all times.

4.23 **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 council 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 council's investment objectives will be monitored regularly.

4.24 **ESG-focussed short term deposits:** Some banks and credit institutions now offer deposit accounts where the funds raised by the banks in these accounts are ring fenced to only be lent on for activities with an ESG focus. Such deposit accounts afford the same protections as other deposits with the bank hence allowing the council to support the ESG agenda whilst acting within the strict requirements for security and liquidity.

4.25 **Operational bank accounts:** The council may incur operational exposures, for example though 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 £9m* per bank. 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 council maintaining operational continuity.

4.26 * It is possible, rarely, that significant amounts of funding (for example government grants) may be received unexpectedly towards the end of a banking day, at which point it is not possible to place these funds with a suitable approved counterparty until the following day. This would not be considered a breach of the £9m limit provided the surplus cash is appropriately invested at the earliest opportunity on the following banking day.

4.27 **Risk assessment and credit ratings**: One of the ways that the council manages credit risk is by using credit ratings.

4.28 The council uses long-term credit ratings from the three main rating agencies, Fitch Ratings Ltd, Moody's Investors Service Inc and Standard & Poor's Financial Services LLC, to assess the risk of investment default. The lowest available credit rating will be used to determine credit quality.

4.29 Long-term ratings are expressed on a scale from AAA (the highest quality) through to D (indicating default). Ratings of BBB- and above are described as 'investment grade', while ratings of BB+ and below are described as 'speculative grade'. The council's credit rating criteria are set to ensure that it is unlikely that the council will hold speculative grade investments, despite the possibility of repeated downgrades.

4.30 Credit ratings are obtained and monitored by the council's treasury advisers on at least a monthly basis, who will notify changes in ratings as they occur.

4.31 **Other Information on the security of investments:** The council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will 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 council'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.

4.32 **Reputational aspects:** The council 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 considered when making investment decisions.

4.33 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 council 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 council'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.

4.34 Investment Limits

4.35 The council's revenue reserves that may be deemed as 'available' and could potentially be called up to cover investment losses should the need arise are forecast to be £70 million on 31st March 2024 and £44 million on 31st March 2025, although it should be noted that these are currently being held for other purposes are would not expect to be needed. In order that no more than 75% 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 £30 million. A group of entities under the same ownership will be treated as a single organisation for limit purposes.

4.36 Credit risk exposures arising from non-treasury investments, financial derivatives and balances in operational bank accounts count against the relevant investment limits.

4.37 Limits are also placed on fund managers 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 6: Additional investment limits

	Cash limit
Any group of pooled funds under the same management	£15m per manager
Foreign countries	£12m per country (£8m in-house & £4m cash-manager)

4.38 Liquidity management

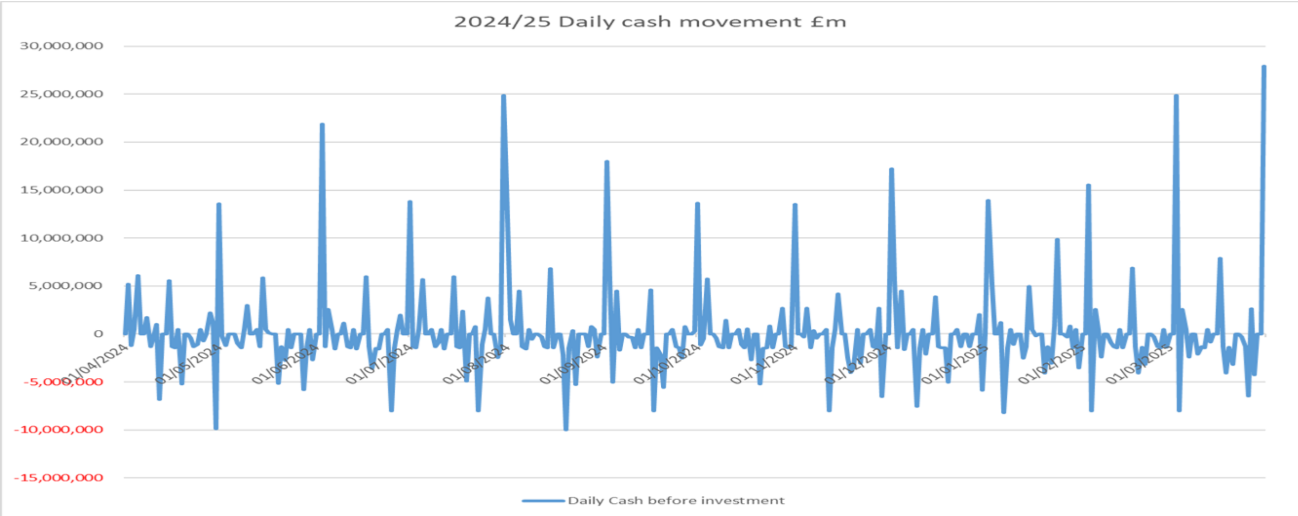
4.39 The council uses a series of control spreadsheets to monitor and forecast the council's cash flows, to determine the maximum period for which funds may prudently be committed, and to manage the council's exposure to liquidity and re-financing risks. The forecast is compiled on a prudent basis, with receipts under-estimated and payments over-estimated to minimise the risk of the council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the council's medium term financial plan and cash flow forecast.

4.40 The council will spread its liquid cash amongst 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.

4.41 The council has an agreed overdraft facility, and access to sources of cash such as borrowing from the PWLB, and other counterparties, such as banks and other local authorities. In addition, the council's investment holdings can be readily realised, if required.

4.42 Management of cash-flows

Table 7: Daily cash-flow movements can be seen in the table below.



4.43 Although the cash-flow movements could be described as fluctuating or potentially even volatile, trends do begin to emerge when the nature of the movements are understood, for example;

- Significant inflows include council tax and business rates income, government grants and subsidy used to support and fund parts of the annual revenue budget including schools, contributions from stakeholders in respect of funding agreements (e.g., health partners), grants and contributions used to fund capital projects. Some of these inflows follow a regular pattern, which may be weekly, bi-weekly, monthly, or quarterly and others do not, they simply arrive into the council's bank accounts.

- Significant outflows include monthly payments to staff, pension providers and government agencies, payments to suppliers 3 times each week covering both revenue and capital spending, payment of housing benefits, payments to major preceptors such as Fire, Police, Environment Agency, Town and Parish councils.

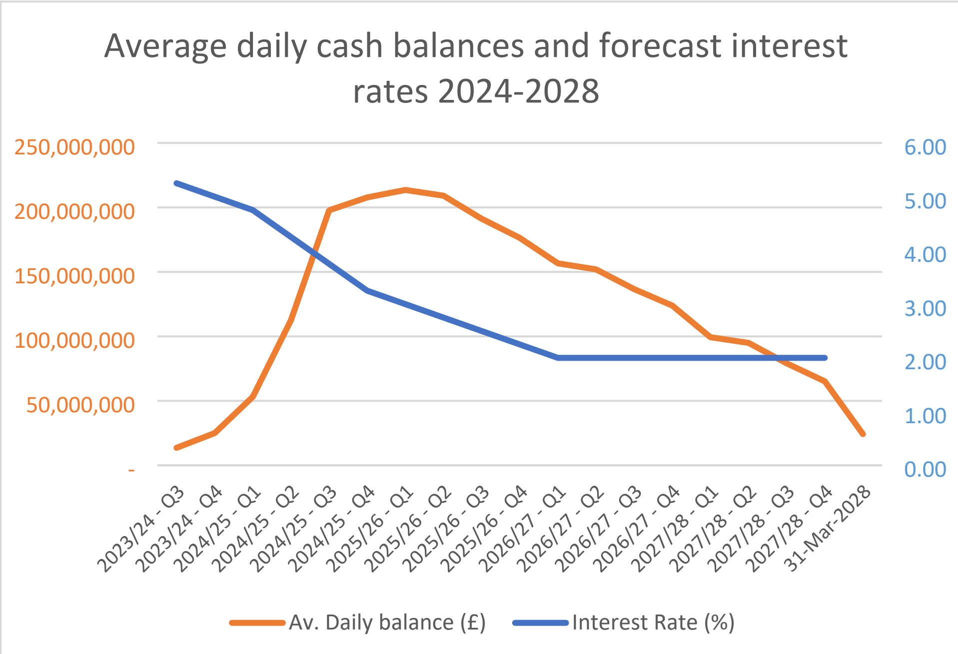
4.44 Over the past three years the council's cash-flows have been significantly impacted by government support packages for both Covid and more recently, the cost of living/ energy pressures, as it has received significant amounts of additional funding and support packages, both in relation to the council's own budget, as well as when it has been acting as an agent for the government by passporting monies onto individuals, suppliers, and businesses.

4.45 Whilst the new capital investment spending totals are anticipated for next year, the spending profiles associated with them have yet to be developed in any detail although it is estimated that less spending will be incurred during the first quarter of the year.

4.46 The annual cash flow principles have been continued across the MTFP period, which has helped support the forecast investment income in the MTFP.

4.47 Table 8 below shows the average daily cash balances increasing as the current investments mature over the next 12 months, and then start to fall over the remaining period.

Table 8: Extended average daily cash balances and interest rate assumptions 2024-2028.



4.48 The intended borrowing strategy for 2024/25 recommends that external borrowing is not taken, but spending will instead be offset against current surplus cash balances, i.e., it will be funded internally, which means that cash-flow forecasts for next year will decrease from current levels.

5 NON-TREASURY INVESTMENT STRATEGY

4.49 This non-treasury management investment strategy focuses on the council's service investments and commercial property investments.

4.50 Service investments: Loans

4.51 Loans to social enterprises and local businesses may potentially be considered where they contribute to the council's overall objectives, through inclusion in the MTFP, treasury management and capital strategies. Where investment in regeneration and infrastructure in North Somerset clearly support local public services, and stimulate local economic growth, financing may also potentially be considered on projects that offer adequate security and returns, subject to the council having sufficient resources available to it at that time.

4.52 The only loan approved to date is an amount of £0.9m lent to a care home provider in 2008. The care provider has subsequently made repayments (including interest) in line with its agreed schedule. The outstanding balance at the time of writing is £0.8m.

4.53 Commercial investments: Property

4.54 The council's Commercial Investment Strategy was approved by Council in January 2019. In line with this strategy, the council has made two investments in commercial property to earn investment income, through a combination of rental and car parking income, whilst potentially providing capital appreciation over the long-term.

4.55 The investments made under the strategy were all agreed in previous years and consist of one outright purchase funded from long term borrowing, the North Worle District Centre, and one property acquired under a finance lease, the Sovereign Centre in Weston-super-Mare. There were no purchases or sale of assets during the 2023/24 financial year and there are no current plans to undertake any further commercial investments in the future.

4.56 In February 2021 the Executive approved a revised Sovereign Centre Business Plan, setting out the challenges, opportunities, and a new vision for the property. As part of this Business Plan, some of the vacant retail space within the centre has been converted into office space to diversify away from pure retail use.

4.57 After servicing costs, fees and borrowing costs, and a £0.1m use of the smoothing reserve, these assets are budgeted to generate an annual net return to the revenue budget of £0.0m (2022/23 £0.0m).

4.58 Commercial property investments are likely to be less liquid than financial investments, as property may take time to sell in certain market conditions. The council's commercial property investments are considered sufficiently proportionate to its overall investment and borrowing balances to not be likely to significantly impact on the council's overall liquidity position.

4.59 The council has no plans to dispose of its commercial investment properties currently.

6 BORROWING STRATEGY

4.60 <u>Local context</u>

4.61 Forecast changes to the capital financing requirement and borrowing forecasts are shown in the balance sheet analysis in the table below. The 2024/25 capital strategy is being developed but will not be complete in time for this report. The TM report to the Executive in February will therefore include the capital financing requirement compared to forecast borrowing table and commentary as well as implications from the capital strategy on the council's borrowing requirement.

4.62 **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) Other Local Authorities and Pension Funds (except the Avon Pension Fund)
c) UK Municipal Bond Agency plc and other special purpose companies created to enable local authority bond issues
d) Funds administered by the West of England Combined Authority including
   i) Revolving Infrastructure Fund
   ii) Local Growth Fund
   iii) Economic Development Fund
e) any institution approved for investments (see above)
f) any other bank or building society on the Financial Services Authority list
g) UK Infrastructure Bank Limited
h) Retail investors via a regulated peer-to-peer platform
i) Any other UK public sector body

4.63 **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) leases
b) private finance initiative schemes
c) sale and leaseback
d) revolving infrastructure grants

4.64 The council's debt portfolio is managed to ensure that the maturity profile will not leave any one future year with a high level of repayments that could present difficulties in refinancing. Fixed rate loans are usually taken to lock into known interest rates, thus protecting against fluctuations and providing certainty when managing and setting the budget.

4.65 Whilst the above deals with past or present borrowing requirements, it is also possible to borrow in advance of need where there is a clear business case for doing so and only for the approved capital programme or to finance future debt maturities, as permitted by the guidance. Borrowing in advance of need introduces additional credit and interest risk. Whilst there is no present intention to borrow in advance, all risks will be considered as part of any borrowing decision, should conditions favour such action.

4.66 Furthermore, 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. The council 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.

7 INTEREST RATES AND ECONOMIC OUTLOOK

4.67 **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.

4.68 The Bank of England (BoE) increased Bank Rate to 5.25% in August 2023, before maintaining this level for the rest of 2023. In December 2023, 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%.

4.69 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 upside risks to CPI falling to the 2% target coming from potential energy price increases, strong domestic wage growth and persistence in price-setting.

4.70 Office for National Statistics (ONS) figures showed CPI inflation was 3.9% in November 2023, down from a 4.6% rate in the previous month and, in line with the recent trend, lower than expected. The core CPI inflation rate declined to 5.1% from the previous month's 5.7%, again lower than predictions. Looking ahead, using the interest rate path implied by financial markets the BoE expects CPI inflation to continue falling slowly, but taking until early 2025 to reach the 2% target before dropping below target during the second half 2025 and into 2026.

4.71 ONS figures showed the UK economy contracted by 0.1% between July and September 2023. The BoE forecasts GDP will likely stagnate through 2024. The BoE forecasts that higher interest rates will constrain GDP growth, which will remain weak over the entire forecast horizon.

4.72 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 has remained strong, but has showed some signs of easing; regular pay (excluding bonuses) was up 7.3% over the period and total pay (including bonuses) up 7.2%. Adjusted for inflation, regular pay was 1.4% 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.

4.73 Having increased its key interest rate to a target range of 5.25-5.50% in August 2023, the US Federal Reserve appears now to have concluded the hiking cycle. It is likely this level represents the peak in US rates following a more dovish meeting outcome in December 2023. 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 the impact from higher rates has started to feed into economic activity and growth will weaken in 2024. Annual CPI inflation was 3.1% in November.

4.74 Eurozone inflation has declined steadily since the start of 2023, falling to an annual rate of 2.4% in November 2023. Economic growth has been weak, and GDP contracted by 0.1% in the three months to September 2023. In line with other central banks, the European Central Bank has increased rates, taking its deposit facility, fixed rate tender, and marginal lending rates to 3.75%, 4.25% and 4.50% respectively.

4.75 **Credit outlook:** 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.

4.76 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.

4.77 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.

4.78 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.

4.79 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.

4.80 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.

4.81 **Interest rate forecast (December 2023):** 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 start reducing rates in 2024 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.

4.82 Arlingclose expects long-term gilt yields to be broadly stable at current levels (amid continued volatility), following the decline in yields towards the end of 2023, which reflects the expected lower medium-term path for Bank Rate. 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.

4.83 A more detailed economic and interest rate forecast provided by Arlingclose is in **Appendix 6.**

4.84 For the purpose of setting the budget, it has been assumed that new short-term treasury investments will be made at an average rate/yield of 4.25%. No new long-term borrowing will be undertaken, which means that interest payments will not be required, although MRP will be a factor.

8 OTHER TREASURY MANAGEMENT MATTERS

4.85 The CIPFA Code requires the council to include the following in its treasury management strategy:

4.86 **Financial Derivatives**: Councils may make 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).

4.87 In line with the CIPFA Code, the council will seek external advice and will consider that advice before entering into financial derivatives to ensure that it fully understands the implications. The council has no plans to make use of financial derivatives in 2024/25.

4.88 **Markets in Financial Instruments Directive:** The council 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 council's treasury management activities, the Section 151 Officer believes this to be the most appropriate status.

1.1 INTRODUCTION

Having adopted both the CIPFA Treasury Management in the Public Services Code of Practice, and the Prudential Code for Capital Finance in Local Authorities, the council is required follow the elements within the Guidance and set 'indicators' which demonstrate that it follows good practice and has implemented and operates within appropriate systems of control before making capital financing and treasury management decisions.

1.2 PRUDENTIAL INDICATORS 'PRUDENTIAL CODE':

The 2024/25 capital strategy is being developed but will not be complete in time for this report. The TM report to the Executive in February will therefore include the prudential indicators. The Treasury Management and investment indicators are included in this report below.

1.3 TREASURY MANAGEMENT INDICATORS: '<u>TREASURY CODE'</u>

The council measures and manages its exposures to treasury management risks using the following indicators.

1.3.1 <u>Security: Credit risk indicator</u>

The council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average 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.

Table 1.3.1: Credit risk indicator:

Credit risk indicator	Target
Portfolio average credit rating	A-

1.3.2 <u>Interest rate exposures</u>

This indicator is set to control the council'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:

Table 1.3.2: Interest rate risk indicator:

Interest rate risk indicator	Limit (£m)
Upper limit on one-year revenue impact of a 1% <u>rise</u> in interest rates	2.0
Upper limit on one-year revenue impact of a 1% <u>fall</u> in interest rates	2.0

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.

1.3.3 <u>Maturity structure of borrowing</u>

Refinancing risk is the risk that a borrower cannot refinance by borrowing to repay existing debt. To address this risk, limits are set of the proportions of the council's borrowing which are due to fall due in specified periods.

Table 1.3.3: Upper & lower limits on borrowing maturities, as a % of total borrowing:

Maturity Structure of Borrowing	Upper	Lower
Under 12 months	50%	0%
12 months and within 24 months	30%	0%
24 months and within five years	40%	0%
5 years and within 10 years	50%	0%
10 years and above	100%	0%

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.

1.3.4 Long-term treasury management investments

The purpose of this indicator is to control the council'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:

Table 1.3.4: Long term treasury management investments in £ millions:

Price risk indicator	2024/25	2025/26	2026/27	No fixed date
Limit on principal invested with maturities longer than 365 days beyond year end	£40m	£40m	£40m	£10m

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

1.4 NON-TREASURY MANAGEMENT INDICATORS: 'INVESTMENT GUIDANCE'

The council has set the following quantitative indicators to allow elected members and the public to assess the council's total risk exposure resulting from its investment decisions.

1.4.1 Total risk exposure

The first indicator below shows the council's total exposure to potential investment losses. This includes amounts the council is contractually committed to lend but have yet to be drawn down and guarantees the council has issued over third-party loans.

Table 1.4.1: Total investment exposure in £ millions

Total investment exposure	Actual Held as at 31/03/23 £m	Forecast Held as at 31/03/24 £m	Forecast Held as at 31/03/25 £m
Treasury management investments	154.0	178.4	197.1
Service investments: Loans	0.8	0.8	0.8
Commercial investments: Property*	23.5	23.5*	23.5*
TOTAL EXPOSURE	**178.3**	**202.7**	**221.4**

** Commercial investment properties are re-valued annually by the council's valuers - valuations as at 31/3/24 are not yet available and cannot be forecast with reasonable certainty.*

1.4.2 How investments are funded

Current government guidance is that these indicators should include how investments are funded. Since the council does not normally associate particular assets with particular liabilities, this guidance is difficult to comply with.

In accordance with best professional practice, North Somerset Council does not associate its borrowing with particular items or types of expenditure. The council manages its treasury position, borrowings, and investments in accordance with its approved Treasury Management Strategy and practices. In day-to-day cash management, no distinction is made between revenue cash and capital cash. External borrowing arises because of all the financial transactions of the council, and not simply those arising from capital spending. The council may choose to finance capital expenditure from its existing operational cash resources, rather than undertaking external borrowing, to minimise interest costs.

1.4.3 Rate of return received on investments

This indicator shows the investment income received less the associated costs, including the cost of borrowing where appropriate, as a proportion of the sum initially invested. Note that due to the complex local government accounting framework, not all recorded gains and losses affect the revenue account in the year they are incurred.

Table 1.4.3: Investment rate of return (net of all costs)

Investments net rate of return	**Actual 2022/23 %**	**Forecast 2023/24 %**	**Forecast 2024/25 %**
Treasury management investments	1.79	4.85	4.85
Service investments: Loans	4.62	7.05	7.05
Commercial investments: Property	1.81	0.00	0.00
ALL INVESTMENTS	**1.85**	**3.68**	**3.68**

Treasury management risk register

Appendix 3

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Risk	Impact	Probability	Unmitigated risk	Mitigating arrangements:	Revised probability	Residual risk
Credit risk						
- Loss of principal and/or interest due to counter-parties not being able to meet principal / interest payments as they fall due. Includes losses due to 'bail in' requirements. - Potential delays in being able to access funds. - Emerging markets carry a higher risk of financial loss than more developed markets, as they may have less developed legal, political, economic or other systems.	5	4	20	- Measurement of risk (use of credit ratings, CDS spreads, balance sheet analysis). - Monitoring of TM advisor advice, news, discussions with brokers, and reacting to events (eg both trading and regulatory). - Setting appropriate lending limits per counter-party re amounts, period and country of investment. - Diversification between lenders, lender types, countries. - Exposure to equity and tradable debt instruments only through diversified funds.	3	15
Liquidity risk						
- Running out of accessible cash, leading to inability to make payments as they are due. - Needing to borrow at higher cost than otherwise available. - Needing to sell assets / investments at short notice / at lower prices. - Not having available counter-parties to invest in.	4	2	8	- Daily cash flow forecasting. - Overdraft facility agreed. - Ready access to sources of cash from eg PWLB, other local authorities and banks and building societies. - Holding investments that can be readily realised.	1	4
Interest rate risk						
- Increasing interest rates lead to increase in cost of fixed rate and variable rate borrowing. - Decreasing market value of tradable fixed income investments (e.g. bonds) when interest rates rise. - Falling interest rates lead to lower return - Re-financing risk - Falling borrowing interest rates mean opportunity to re-finance borrowing at lower cost missed. - The use of derivatives may increase overall risk, by magnifying the effect of both gains and losses, leading to large changes in value and potentially large financial loss.	4	5	20	- Monitoring of TM advisor advice, news, discussions with brokers re economic outlook, and expected interest rate movements. - Taking into account uncertainty in future outcomes. - Monitoring of available / emerging sources of borrowing. - Maintaining suitable mix of fixed and variable interest rates for borrowing and investments. - Maintaining mix of maturity dates. - Monitoring of cost of re-financing borrowing compared to potential savings - Diversification of investment types. - Exposure to tradable debt instruments only through diversified funds. - Restriction of use of derivatives to stand-alone instruments that can be clearly demonstrated to reduce overall risk.	4	16
Inflation risk						
- The value of cash balances is eroded over time due to inflation (notably when interest rates on investments are lower than inflation)	4	4	16	- Monitoring of TM advisor advice, news, discussions with brokers re economic outlook, and expected inflation and related interest rate movements. - Identify balances not likely to be needed in the short term for operational cash flows, and invest these balances in longer term to generate sufficient income to at least match inflation.	3	12
Currency risk						
- The risk of loss from fluctuating foreign exchange rates when an investor has exposure to foreign currency or in foreign-currency-traded investments	1	0	0	- Local authorities are not allowed to borrow or invest in foreign currencies. All transactions must be in sterling.	0	0
Regulatory and political risk						
Risk that changes in regulations or leglislation may have an adverse impact on the Council's finances, including: - Brexit - leads to uncertainty in the economic outlook, and hence uncertainty over future interest rates and economic growth, and hence inflation, and government expenditure. - Changes in PWLB / other borrowing rates impact on the Council's borrowing costs - Changes in PWLB regulations limit availability/criteria of borrowing. - Changes in MiFID 2 regulatory requirements may increase costs and decrease access to markets.	3	4	12	- Monitoring of TM advisor advice, news, discussions with brokers, and reacting to events (eg both trading and regulatory). - On-going professional training and development of treasury management officers. - On-going training and updates to members on Treasury Management. - Regular review and update of overall Treasury Management Strategy. - Regular review and update of mix of borrowing and investments held to ensure the portfolio continues to meet the objectives of the Treasury Management Strategy.	3	9

Key: Scores: 1 (Lowest)-5 (Highest)

ESG Investment Policy

1.1 The council has developed the following framework for Environmental, Social and Governance (ESG) considerations and incorporated this ESG investment policy within the 2024/25 treasury management strategy.

1.2 CIPFA Treasury Management Code 2021 includes the requirement that a council's credit and counterparty policies should set out its policies and practices relating to ESG investment considerations, although it is not implied that this policy will currently include ESG scoring or other real-time ESG criteria at individual investment level.

1.3 The ESG investment policy will not detract from the core functions that need to take place within the existing treasury management strategy, i.e., the management of cash-flows and meeting the requirements within the approved revenue budget. The policy ensures that climate and other environmental implications are considered and reported on.

1.4 The council will continue to;

- avoid any direct treasury investments in companies related to fossil fuel exploration and extraction;

- engage with advisors to explore and assess the potential for any future investment opportunities in funds with a renewable energy & sustainability focus;

- maintain funds placed in a "Green Deposit Account," which is an investment facility that ensures deposits are linked to a wide range of projects in the pursuit of transition to a lower carbon economy. These projects cover a variety of themes including energy efficiency renewable energy, green transport, sustainable food, agriculture and forestry and greenhouse gas emission reductions.

1.5 In addition to the above, the ESG Investment policy includes the following set of ESG principles:

- The council's ESG investment policy must still be compliant with the external and internal regulatory framework, and will therefore continue to give focus to security and liquidity, then yield.

- When investing in banks, the council will seek to prioritise banks that are signatories to the UN Principles for Responsible Banking and the Net Zero Banking Alliance;

- When investing in funds, the council will seek to prioritise funds operated by managers that are signatories to the UN Principles for Responsible Investment, the UK Stewardship Code and/or the Net Zero Asset Managers Alliance;

- Direct involvement and financing of green energy projects is treated as capital expenditure, and as such is not covered within the remit of treasury management.

1.6 The signatories, principles, and alliances referred to above are referred to in more detail in para 4.12 below.

ESG investment strategy 2024/25

1.7 The following ESG investment strategy is proposed for adoption in 2024/25;

- To set aside an initial sum of up to £6m to invest specifically in ESG-related investments;
- Counterparty value and term limits will still be adhered to – for example if the counterparty limit in the approved strategy is £10m then this limit includes both ESG and non-ESG investment products;
- The duration of ESG investment to be less than 12 months – the council is expected to have a borrowing requirement in the next 2-5 years therefore a longer term ESG investment would not be suitable.

ESG Liquidity investing options

1.8 The council recognises there are few options for ESG liquidity investing, and in addition to the principles above will also consider investment in the following:

- HSBC Sterling ESG Liquidity Fund considers ESG criteria in its investment selection;
- Local authorities and housing associations (subject to suitable due diligence).

Local authorities and housing associations

1.9 Housing associations are usually charitable organisations that attempt to meet the UK's social housing needs.

1.10 Local authorities act under statute to meet the societal requirements of residents, including education, welfare for less able/disadvantaged groups, social housing, etc.

Reporting

1.11 The performance of the council's ESG investments will be reported within the various treasury management reports to the Audit Committee during 2024/25.

UN Principles, Net Zero Alliances, and the UK Stewardship Code

1.12 When investing in banks or funds, the ESG investment policy refers to signatories of various UN principles, the UK stewardship code or membership of Net Zero alliances. Additional information about each of these ESG initiatives is included below.

Investing with banks - UN Principles for Responsible Banking (UNPRB)

1.13 The aim of the UN Principles for Responsible Banking is to accelerate a positive global transition for people and the planet.

1.14 It has over 330 signatories with total assets of c.US$84 trillion, representing over half of global banking industry (data as at Dec-23). Through the Principles, outlined below, banks take action to align their core strategy, decision-making, lending, and investment with the UN Sustainable Development Goals (UN SDGs), and international agreements such as the Paris Climate Agreement.

1.15 The six Principles are:

- Alignment with the UN SDGs, the Paris Agreement, and relevant national and regional frameworks;
- Continuously increasing positive impacts while reducing the negative impacts on people and the environment resulting from the bank’s activities, products, and services;
- Working responsibly with clients and customers to encourage sustainable practises and enable economic activities that create shared prosperity for current and future generations;
- Proactively and responsibly consulting, engaging, and partnering with relevant stakeholders to achieve society’s goals;
- Committing to the Principles through effective governance and a culture of responsible banking;
- Being transparent and accountable for the bank’s positive and negative impacts and contribution to society’s goals.

Investing with banks - Net-Zero Banking Alliance

1.16 The Net-Zero Banking Alliance was launched in April 2021 by 43 founding members and has since grown to about 40% of global banking assets. The Alliance supports the implementation of decarbonisation strategies, providing an internationally coherent framework and guidelines in which to transition of the real economy to net-zero emissions.

1.17 Banks commit to:

- Transition the operational and attributable GHG emissions from their lending and investment portfolios to align with pathways to net-zero by 2050 or sooner;
- Within 18 months of joining, set 2030 targets (or sooner) and a 2050 target, with intermediary targets to be set every 5 years from 2030 onwards;
- Focus their first 2030 targets on priority sectors where the bank can have the most significant impact, i.e., the most GHG-intensive sectors within their portfolios, with further sector targets to be set within 36 months;
- Annually publish absolute emissions and emissions intensity in line with best practice and within a year of setting targets, disclose progress against a board-level reviewed transition strategy setting out proposed actions and climate-related sectoral policies;
- Take a robust approach to the role of offsets in transition plans.

Fund managers (MMFs and strategic funds) - UN Principles for Responsible Investment (UN PRI)

1.18 The United Nations defines Responsible Investment as “a strategy and practice to incorporate environmental, social and governance factors in investment decisions and active ownership,” complementing traditional financial analysis and portfolio construction techniques.

1.19 The UN’s Principles of Responsible Investment (PRI) promote the incorporation of ESG into investment decision-making. Its approach is outlined in six guiding principles for investors in their role as asset owners.

- incorporation of ESG issues;
- active ownership;
- seeking appropriate disclosure on ESG issues from investee entities through the Global Reporting Initiative;
- wider promotion of the principles in the investment industry;
- working together to enhance effectiveness; and
- reporting on activities and progress made.

Fund managers (MMFs and strategic funds) - The UK Stewardship Code

1.20 The UK Stewardship Code 2020 views active ownership as the “responsible allocation, management and oversight of capital to create long-term value for clients and beneficiaries leading to sustainable benefits for the economy, the environment and society”.

1.21 The Code has a strong focus on stewardship activities and outcomes. It expects signatories to progress beyond articulating their stewardship policies and comprises a set of “apply and explain” principles, to boost transparency and disclosure. The Code’s 12 principles focus on "Purpose and Governance", "Investment Approach", "Engagement" and "Exercising Rights and Responsibilities".

1.22 Signatories to the 2020 Code report annually with specific evidence for each reporting period on the Code’s application, including activities and outcomes, successes, and setbacks, all described succinctly and in plain English.

Fund managers (MMFs and strategic funds) - Net-Zero Asset Managers initiative

1.23 Launched in December 2020 and now with 315+ signatories with US$57 trillion of assets under management (04-Dec-23), its goal is to accelerate the transition towards global net-zero emissions by 2050 and for asset managers to play their part in helping deliver the goals of the Paris Agreement and ensuring a just transition. Managers also support investing aligned with net zero emissions by 2050 or sooner.

1.24 The commitments of this initiative include setting interim targets for 2030. Managers will be accountable through their annual climate-related financial disclosures and their climate action plan. It does not mean that asset managers will need to divest a given asset as engagement and stewardship are important levers and may have more impact on real economy emissions than by simply divesting.

Authorised Limit – the maximum amount of external debt at any one time in the financial year.

Bank Rate – the Bank of England base rate.

Capital Financing Requirement – financing needs of the council – i.e., the requirement to borrow.

CIPFA - the Chartered Institute of Public Finance and Accountancy. The institute is one of the leading professional accountancy bodies in the UK and the only one which specialises in the public sector. It is responsible for the education and training of professional accountants and for their regulation through the setting and monitoring of professional standards. Uniquely among the professional accountancy bodies in the UK, CIPFA has responsibility for setting accounting standards for a significant part of the economy, namely local government. CIPFA's members work, in public service bodies, in the national audit agencies and major accountancy firms.

CLG – Communities and Local Government – see MHCLG.

Counterparty – the organisation the council is investing with.

Credit Rating – an assessment of the credit worthiness of an institution.

Creditworthiness – a measure of the ability to meet debt obligations.

ESG – Environmental, Social and Governance based investment decisions.

Finance Lease - a finance lease is a lease that is primarily a method of raising finance to pay for assets, rather than a genuine rental. The latter is an operating lease. The key difference between a finance lease and an operating lease is whether the lessor (the legal owner who rents out the assets) or lessee (who uses the asset) takes on the risks of ownership of the leased assets. The classification of a lease (as an operating or finance lease) also affects how it is reported in the accounts.

Gilts – long term fixed income debt security (bond) issued by the UK Government and traded on the London Stock Exchange.

LIBID – London Interbank BID Rate – the interest rate at which London banks are willing to borrow from one another.

MHCLG – Ministry of Housing, Communities and Local Government. The Government department that sets policy on supporting local government, communities and neighbourhoods, regeneration, housing, planning building and the environment and fire. The name for this Government department has recently changed and is now known as **DLUHC**, which is the **Department for Levelling Up, Housing and Communities**.

Minimum Revenue Provision - the minimum amount which must be charged to an authority's revenue account each year and set aside towards repaying borrowing.

Money Market - the market in which institutions borrow and lend.

Money Market Rates – interest rates on money market investments.

Ninety-One – one of the council's cash managers who invest in multi-asset funds. They were previously known as Investec.

Operational Boundary – the most likely, prudent but not worst-case scenario of external debt at any one time.

Pooled Funds – investments are made with an organisation who pool together investments from other organisations and apply the same investment strategy to the portfolio. Pooled fund investments benefit from economies of scale, which allows for lower trading costs per pound, diversification, and professional money management.

Prudential Code – a governance procedure for the setting and revising of prudential indicators. Its aim is to ensure, within a clear framework, that the capital investment plans of the council are affordable, prudent, and sustainable and that treasury management decisions are taken in accordance with good practice.

Prudential Indicators – indicators set out in the Prudential Code that calculates the financial impact and sets limits for treasury management activities and capital investment.

PWLB (Public Works Loans Board) - a central government agency which provides long and medium-term loans to local authorities at interest rates only slightly higher than those at which the Government itself can borrow. Local authorities can borrow to finance capital spending from this source.

Sovereign – the countries the council can invest in.

Tradition UK Ltd – is one of the council's cash managers who manage £10m of investments on our behalf. Tradition place funds in fixed term cash deposits with a range of financial institutions.

Treasury Management – the management of the council's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risk associated with those activities and the pursuit of optimum performance with those risks.

Treasury Management Practices – schedule of treasury management functions and how those functions will be carried out.

Variable Net Asset Value money market funds – the principal invested may fluctuate below that invested.

1.1 Underlying assumptions:

1.2 UK inflation and wage growth remain elevated but have eased over the past two months fuelling rate cuts expectations. Near-term rate cuts remain unlikely, although downside risks will increase as the UK economy likely slides into recession.

1.3 The MPC's message remains unchanged as the Committee seeks to maintain tighter financial conditions. Monetary policy will remain tight as inflation is expected to moderate to target slowly, although some wage and inflation measures are below the Bank's last forecasts.

1.4 Despite some deterioration in activity data, the UK economy remains resilient in the face of tighter monetary policy. Recent data has been soft but mixed; the more timely PMI figures suggest that the services sector is recovering from a weak Q3. Tighter policy will however bear down on domestic and external activity as interest rates bite.

1.5 Employment demand is easing. 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 and business spending will therefore be weak.

1.6 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.

1.7 Maintaining monetary policy in restrictive territory for so long, when the economy is already struggling, will require significant loosening in the future to boost activity.

1.8 Global bond yields will remain volatile. Markets are currently running with expectations of near-term US rate cuts, fuelled somewhat unexpectedly by US policymakers themselves. Term premia and bond yields have experienced a marked decline. It would not be a surprise to see a reversal if data points do not support the narrative, but the current 10-year yield appears broadly reflective of a lower medium-term level for Bank Rate.

1.9 There is a heightened risk of fiscal policy and/or geo-political events causing substantial volatility in yields.

1.10 Forecast:

1.11 The MPC held Bank Rate at 5.25% in December. We believe this is the peak for Bank Rate.

1.12 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.

1.13 The immediate risks around Bank Rate have become more balanced, due to the weakening UK economy and dampening effects on inflation. This shifts to the downside in the short term as the economy weakens.

1.14 Long-term gilt yields are now substantially lower. Arlingclose expects yields to be flat from here over the short-term reflecting medium term Bank Rate forecasts. Periodic volatility is likely.

	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	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	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	0.00	0.25	0.25	0.50	0.50	0.50	0.50	0.50	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	0.25	0.75	0.85	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	3.77	3.75	3.75	3.75	3.70	3.60	3.50	3.50	3.40	3.30	3.30	3.30	3.35
Downside risk	0.00	-0.25	-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	0.25	0.75	0.85	0.85	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	3.72	3.75	3.80	3.80	3.80	3.80	3.80	3.80	3.75	3.65	3.60	3.65	3.70
Downside risk	0.00	-0.25	-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	0.25	0.75	0.85	0.85	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	4.16	4.20	4.20	4.20	4.20	4.20	4.20	4.20	4.20	4.20	4.20	4.20	4.25
Downside risk	0.00	-0.25	-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	0.25	0.75	0.85	0.85	0.90	1.00	1.00	1.00	1.00	1.00	1.00	1.00
Central Case	3.76	3.80	3.85	3.90	3.90	3.90	3.90	3.90	3.90	3.90	3.95	3.95	3.95
Downside risk	0.00	-0.25	-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%

North Somerset Council

Report to the Audit Committee

Date of Meeting: 25 January 2024

Subject of Report: Update on Annual Accounts

Town or Parish: All

Officer presenting: Steve Ballard - Principal Accountant (Closure and Systems)

1. Key Decision: N/A

Recommendations

The Audit Committee are requested to **note** the following:

a) the developments in the CIPFA Code of Practice for Local Government Accounts, including that there are limited changes to the Code for the 2023/24.

b) that officers are proposing no significant changes to existing accounting policies in 2023/24.

c) that officers' initial assessment of the critical judgements made in applying the Council's accounting policies, and the major sources of estimation uncertainty identified in the preparation of the 2023/24 accounts.

d) the requirement for the Council's accounts to provide a 'true and fair' view of the Council's financial position and transactions, the concept of materiality, the initial assessment of materiality limits applied by officers in drawing up the accounts; and disclosures which, although not material due to their value, are considered material due to their nature.

1. Summary of Report

1. The purpose of this report is to provide Members with an update of the issues which impact on the annual accounts process. These include changes to the Code, and the annual review the Council's accounting policies.

2. The report also provides Members with a reminder of the concept of materiality, and outlines officers approach in applying materiality in preparing the draft financial statements.

2. Policy

3. Local authorities in the United Kingdom are required to prepare their accounts in accordance with primary legislation, such as the Accounts and Audit Regulations, as well as 'proper accounting practices', meaning compliance with the terms of the Code of Practice on Local Authority Accounting in the United Kingdom (the Code).

4. The Code specifies the principles and practices of accounting required to prepare a Statement of Accounts which gives a 'true and fair' view of the financial position and transactions of a local authority. The Code is updated annually, and may introduce new, or amended, accounting standards or reporting requirements which need to be complied with.

5. The Audit Committee is charged with overseeing the Authority's financial reporting process, and is required to consider and, under delegated powers from the full Council, to approve the Council's Statement of Accounts each year.

6. The Chair of the Audit Committee and the Chief Financial Officer are required to sign the Council's Statement of Accounts as representing a 'true and fair' view of the financial position of the Council and its income and expenditure for the year.

7. The Chief Financial Officer is responsible for:
   - the preparation of the Statement of Accounts in accordance with the Code,
   - selecting suitable accounting policies and then applying them consistently,
   - making judgements and estimates that are reasonable and prudent,
   - arrangements for internal control as she determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and
   - for being satisfied that the financial statements give a true and fair view of the financial position and transactions of the Council.

8. Audit Committee members therefore need to consider whether they receive adequate assurance over Council's arrangements for the preparation of the financial statements, including arrangements for making critical judgements in applying accounting policies, and for making accounting estimates, before approving the financial statements.

3. Update on the Council's Annual Accounts

Changes to the Code – 2023/24 and 2024/25

9. The Code of Practice is updated annually to reflect new or updated accounting standards. There are only minor changes to the Code for 2023/24. Following review, none are considered likely to have a significant impact on the Council's accounts.

10. CIPFA has confirmed that adoption of IFRS16 – 'Leases' will be mandatory under the Code in 2024/25. This change of accounting policy will require changes to the accounting treatment where the Council is the lessee of long-term assets, and revisions to the related disclosures. Although the implementation of the new standard will be only reflected in the 2024/25 accounts, disclosure of the likely impact of this change will need to be included in the 2023/24 accounts. Work is on-going to quantify the impact of these changes.

11. There is a consensus that the length and complexity of the accounts produced under the current Code can make the accounts impenetrable to many users. CIPFA consulted on

changes to the Code for 2021/22, with the aim of delivering accounts that more clearly communicate the authority's financial performance and future financial sustainability. However, no significant changes have yet been proposed in the Code. CIPFA is continuing to develop guidance on revised content for inclusion in the Code in future years. Officers will continue to seek to simplify and focus the Narrative Report and financial statements on key messages.

12. As in previous years, officers will be holding a workshop to remind members of their core duties in relation to the accounts, the sources of assurance they have available, and to discuss the key messages and financial information contained in the 2023/24 accounts.

Changes to regulatory requirements

13. There are no new regulatory developments outside of the Code that are likely to impact on the 2023/24 financial statements. Issues reported in 2022/23, which remain current, include:
    - Minimum Revenue Provision (MRP) – The Minimum Revenue Provision is the minimum amount which must be charged to a Council's revenue account each year and set aside as provision for repayment of debt, as required by the Local Government Act 2003. Government have issued further guidance on the calculation of the MRP. Officers believe that the Council already makes prudent provision for the repayment of its debt, and therefore does not expect this guidance to significantly impact on the charges the Council makes in its accounts.
    - IFRS 9 Statutory Override for pooled investments –the IFRS 9 statutory override in local government has been extended until 31 March 2025. This provides permission for gains and losses on pooled investments, such as those held by the Council, to continue to be held in Balance Sheet reserves, rather than impacting on the Council's surplus or deficit for the year each year.
    - Dedicated Schools Grants deficits – Similarly, the statutory override for Dedicated Schools Grant (DSG) deficits has been extended to 2025-26.

14. Officers are due to attend technical update training in the next few weeks and will continue to keep Members informed of any significant changes in Code requirements for the content and format of the Council's accounts.

Review of accounting policies

15. Accounting policies are the specific principles and practices applied by an authority in preparing and presenting its financial statements. The finance team has developed a 'library' of the Council's accounting policies. Of these, only those with significant impact are disclosed within the Council's accounts.

16. It is good practice for 'those charged with governance' (i.e. the members of the Audit Committee) to review the policies on an annual basis and approve any changes proposed.

17. Officers have reviewed the Council's library of accounting policies. No significant changes have been made to the Council's accounting policies included in the library of policies.

18. No significant changes are proposed to existing accounting policies over those included in the previous year's statement of accounts.

Accounts which provide a 'true and fair' view of the Council's financial position and transactions, and the concept of materiality

19. Detailed consideration of the assessment of appropriate materiality levels for the Council's preparation of the accounts is set out in Appendix A.

20. Officers consider that it is appropriate to set an indicative materiality level in preparing the Council's accounts at approximately one third of the external auditor's materiality, i.e. based on 2 % of gross revenue expenditure at 'Cost of services' level in the previous years' audited accounts. This equates to around £8.35m.

21. Disclosures which, although not material due to their value, are considered material by their nature, due to their potential impact on the decisions of likely users of the accounts, are:
    a) disclosures of officers' remuneration, salary bandings and exit packages
    b) disclosure of members' allowances
    c) disclosure of related party transactions

Critical judgements made in applying the Council's accounting policies, and major sources of estimation uncertainty in the preparation of the accounts

22. Officers have completed an initial assessment of the critical judgements made in applying the Council's accounting policies, and the major sources of estimation uncertainty identified in the preparation of the 2023/24 accounts. These issues impact on whether the accounts provide a 'true and fair' view of the Council's financial position. These are listed in Appendix B and C respectively.

23. The judgements proposed remain as detailed in the 2022/23 statement of accounts.

24. Each year, members of the Audit Committee participate in a workshop session to review the draft annual financial statements. This provides an opportunity for officers to explain the accounting estimates used in preparing the accounts, and for members to question officers on the adequacy of the Council's arrangements for making accounting estimates.

25. Papers will be submitted to the Audit Committee later in the year setting out the detail of these issues, and the sources of assurance that members can use in making their assessment of the adequacy of the Council's arrangements to produce 'true and fair' financial statements.

4. Consultation

26. Officers continue to undertake discussions with external audit regarding key issues impacting on the preparation of the accounts, including significant accounting estimates and judgements. Officers will continue to liaise with external audit on emerging issues as the accounts are finalised.

5. Financial Implications

27. Updates to the Code, and any proposed changes to the Council's accounting policies, are expected to have minimal impact on the Council's financial out-turn or balances.

28. As noted in Appendices B and C, critical judgements made in applying the Council's accounting policies, and accounting estimates used in the valuation of the Council's assets and liabilities will have a material impact on the Council's financial statements.

6. Legal Powers and Implications

29. The CIPFA Code of Practice determines 'proper accounting practice' in relation to the Council's statement of accounts. The Council's accounts are a key requirement of its operational responsibilities. Their accuracy and adherence to legislation and relevant guidance are important to ensure the Chief Financial Officer and Audit Committee can discharge their statutory obligations.

7. Climate Change and Environmental Implications

30. None.

8. Risk management

31. Failure to apply appropriate accounting policies, or to adequately assess materiality in relation to the Council's accounts, could result in the accounts not providing a 'true and fair view' of the Council's financial position, financial performance and cash flows, and leave the Council open to criticism by external audit, and potential qualification of their audit opinion on the accounts.

9. Equality Implications

32. None.

10. Corporate Implications

33. None, other than as highlighted above.

11. Options Considered

34. Options considered in the update of accounting policies, and in setting materiality levels, are detailed in the body of the report above.

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Appendices

Appendix A   Assessment of materiality
Appendix B   Critical judgements in applying the Council’s accounting policies
Appendix C   Significant accounting estimates and sources of estimation uncertainty

Background Papers

CIPFA Code of Practice on Local Authority Accounting 2023/24
CIPFA Guidance Notes for Practitioners 2023/24
Statement of Accounts 2022/23
Grant Thornton Audit Findings Report 2022/23

Appendix A

Assessment of materiality

1. Introduction

The CIPFA Code of Practice for Local Government accounting specifies the accounting practices required for the Council's Statement of Accounts to give a 'true and fair' view. However, 'true and fair' does not mean 100% accurate, but 'materially correct'.

The Code provides a definition of materiality, which is applied to information and disclosures in the Council's financial statements: "information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific local authority."

The assessment of materiality helps officers to ensure that the accounts focus on key messages, notably in relation to the Council's performance, financial resilience and accountability for use of public funds.

2. Users of the accounts

The assessment of materiality is affected by the financial information needs of users of the financial statements.

The Code defines the primary users of local authority financial statements as 'service recipients and their representatives, and resource providers and their representatives'.

'Service recipients and their representatives' are likely to consist of local residents and their locally elected representatives. 'Resource providers and their representatives' are likely to mean central government, and local Council Tax and Non-domestic rates payers.

Other users are likely to include existing and potential lenders, credit ratings agencies, financial advisors, the media, trade unions, statisticians, analysts and academics, and businesses considering entering contracts with the Council.

In the public sector, providing information that allows for an assessment of the stewardship and accountability of elected members and management for the resources entrusted to them is of paramount importance.

Ensuring that the Council's audited financial statements focus on the needs of key users of the accounts is challenging, as different stakeholder groups will be interested in different information, have differing expectations of whether a particular transaction is material, and will have differing levels of financial literacy.

Hence, engagement with members, through the Audit Committee, provides a useful opportunity of officers to gain an understanding of the content of the financial statements which are likely to influence the decisions of members as users of the accounts.

3. Benchmarks for determining overall materiality

Determining a value for materiality involves the exercise of judgement. A percentage of a chosen benchmark in the accounts is often applied as a starting point. Appropriate benchmarks might include the total assets, liabilities, income, or expenditure in the accounts. As a public sector entity, other benchmarks used in the private sector such as profit before tax, gross profit, revenue and equity, are of limited relevance.

As the Council has custody of public assets to deliver services, the value of long-term assets might be considered an appropriate benchmark. Similarly, the Council holds long-term borrowing to finance its long-term assets. However, a materiality based on these measures alone would not be considered relevant to the wider financial performance of the Council reflected in the financial statements.

Council budgets are set and monitored based on net revenue expenditure (ie gross expenditure less gross income). However, use of net expenditure does not fully reflect the income and expenditure transactions, and hence is considered to lead to too low a materiality level to be meaningful.

The overall benchmark considered to be most relevant to users of the accounts is gross revenue expenditure, as it reflects both the revenue expenditure and income for the year, and can meaningfully be applied when considering entries in the Council's Balance Sheet.

4. External auditor's assessment of materiality

In conducting their audit of financial statements, the Council's external auditor seeks to obtain reasonable assurance about whether the financial statements are free from material misstatement, whether due to fraud or error, thereby enabling the auditor to express an opinion on whether the financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Auditors are required to determine their assessment of materiality for the financial statements as a whole.

In their Audit Findings Report for 2022-23, the Council's external auditors quantified their **overall materiality at £8.35 million** (being approximately 2% of gross revenue expenditure at 'Cost of services' level in the audited 2022-23 accounts).

Note that this provides a lower measure of materiality than that based on a similar percentage of gross revenue expenditure at 'Surplus / deficit on provision of services' level, which includes the impact of financing expenditure and one-off expenditure on losses on disposal of non-current assets. It can be argued that the inclusion of such expenditure might mask the reflection of the cost of the provision of the Council's services in the accounts.

The external auditor's assessment of materiality is a key benchmark in determining the Council's overall materiality level when preparing the draft accounts.

There is a risk that more than one non-material error or omission could be material to the accounts when considered in aggregate. Hence external auditors also set a 'performance materiality', at a level less than the overall materiality, to reduce to an appropriately low level the probability that the aggregate of uncorrected errors and omissions exceeds materiality for the financial statements as a whole.

External auditors typically quantify 'performance materiality' in the range of 50-75% of overall materiality to direct their audit testing. The assessment of performance materiality is typically based on a risk assessment, including:

- an assessment of the past experience of errors identified in the Council's accounts
- the knowledge, experience and continuity of the Council's financial reporting team
- the strength of the Council's overall control environment, including anti-fraud arrangements, and wider IT environment
- the strength of the Council's key financial reporting systems

In their Audit Findings Report for 2022-23, the Council's external auditors quantified their **'performance' materiality at £6.25 million**, being 75% of their overall materiality level.

5. Council's assessment of materiality

The Council needs to provide sufficient assurance to the external auditors that the financial statements are materially correct. Hence it is appropriate for the Council to take in to account the auditor's assessment of materiality when setting its own materiality in preparing the draft accounts.

Setting a materiality limit too high could lead to a risk of omission of information which might influence the user of the accounts, which could lead to the Council's accounts being qualified by their auditors. As the Council's accounts have previously been given unqualified audit opinions by the auditor, it is reasonable to assert that officers' assessment of materiality has not been too high in previous years.

Setting too low a materiality limit would not lead to a risk of qualification, but could lead to:

- excessive detail and 'clutter' being included in the accounts, detracting from the clarity of the key messages being communicated, and
- additional officer and auditor time being required to prepare and audit the accounts when deadlines are already tight.

The Council has a history of producing high quality, accurate draft financial statements. The Council's financial reporting team have strong knowledge and experience of local government accounting, and accounts closure issues. The Council's overall control environment is considered strong, with no significant internal control weaknesses, including in relation to the Council's key financial systems, reported by the external auditors in their Audit Findings Reports, or by Internal Audit in the Annual Governance Statements, in recent years.

It is therefore considered appropriate to set the Council's performance materiality level in preparing the accounts at one third of the external auditor's materiality, such that three such errors, impacting in the same direction, would be needed to lead to a misstatement material to the external auditor's opinion.

This gives a value of overall materiality to be used as a guideline by officers in drafting the Council's 2022/23 accounts of **£8.35m**, and a performance materiality estimated at **£2.78m.**

6. Items which are material by nature

Officers drawing up the accounts, and auditors undertaking the audit of the accounts, may identify classes of transactions, account balance or disclosures which are considered more likely to influence the user of the accounts, and hence where it may be appropriate to set a lower materiality level than for the financial statements as a whole.

Officers have reviewed the statement of accounts, including the associated disclosures, for other items which would be most likely to impact on the decisions of likely users of the accounts, notably local residents. Disclosures identified as 'material by nature' are:

- Officers' remuneration, salary bandings and exit packages
- Members' allowances - as of interest to local residents, and
- Related party transactions –to ensure transparency of the Council's transactions with bodies or individuals who have control or influence over the Council.

Hence these disclosures will be retained in future statement of accounts, despite being below the numerical value of the materiality for the accounts as a whole.

Other disclosures below the Council's materiality threshold, and which are not considered material by nature, will be considered for removal to 'de-clutter' the accounts, and allow better focus on the key messages in the accounts.

Appendix B

Critical judgements in applying the Council's accounting policies

In applying its accounting policies, the Council has had to make judgements about complex accounting transactions.

The critical judgements currently identified by officers are:

- the accounting treatment of grant funding,
- the accounting treatment of Better Care Funding,
- the accounting treatment of schools' non-current assets, and
- the classification of the Council's commercial investment property.

Appendix C

Significant accounting estimates and sources of estimation uncertainty

The Statement of Accounts contains estimated figures that are based on assumptions made by the Council about the future or that are otherwise uncertain. Estimates are made considering historical experience, current trends and other relevant factors.

There have been no significant changes to the basis of these estimates compared to the previous year.

The areas of the accounts which are subject to material accounting estimates, or significant estimation uncertainty are currently assessed as follows:

- investment property valuations, including impairments,
- property, plant and equipment valuations, including impairments, and
- the pension fund (LGPS) net liability valuation, and actuarial gains and losses. Note that a triennial revaluation of the pension fund assets and liabilities was last undertaken by the actuary in 2022/23.

Other areas where accounting estimates are used, but considered less likely to have a material impact include:

- estimated remaining useful lives of PPE / depreciation and amortisation,
- measurement of financial instruments,
- bad debt provisions / credit loss allowances,
- provisions for liabilities, and
- accruals.

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