

04 September 2017

AUDIT AND STANDARDS COMMITTEE

A meeting of the Audit and Standards Committee will be held on **TUESDAY 12 SEPTEMBER 2017** in the Council Chamber, Ebley Mill, Ebley Wharf, Stroud at **7.00 pm.**



David Hagg
Chief Executive

Please Note: This meeting will be filmed for live or subsequent broadcast via the Council's internet site (www.stroud.gov.uk). By entering the Council Chamber you are consenting to being filmed. The whole of the meeting will be filmed except where there are confidential or exempt items, which may need to be considered in the absence of the press and public.

AGENDA

1. **APOLOGIES**
To receive apologies for absence.
2. **DECLARATIONS OF INTEREST**
To receive declarations of interest.
3. **MINUTES**
To approve the minutes of the meeting held on 4 July 2017.
4. **PUBLIC QUESTION TIME**
The Chair of Committee will answer questions from members of the public submitted in accordance with the Council's procedures.
DEADLINE FOR RECEIPT OF QUESTIONS
Noon on THURSDAY 7 SEPTEMBER 2017.
Questions must be submitted in writing to the Chief Executive, Democratic Services, Ebley Mill, Ebley Wharf, Stroud and sent by post or by Email: democratic.services@stroud.gov.uk.
5. **WORK PROGRAMME**
To consider the work programme.

6. **EXTERNAL AUDIT REPORT 2016/17**
To consider KPMG's External Audit Report 2016/17.
7. **STATEMENT OF ACCOUNTS 2016/17**
To approve the statement of accounts 2016/17 and receive KPMG's audit opinion.
8. **INTERNAL AUDIT ACTIVITY PROGRESS REPORT 2017/18**
To inform Members of the Internal Audit activity progress in relation to the approved Internal Audit Plan 2017/18.
9. **1ST QUARTER TREASURY MANAGEMENT ACTIVITY REPORT 2017/18**
To provide an update on treasury management activity as at 30 June 2017.
10. **MEMBERS' QUESTIONS**
See Agenda Item 4 for deadline for submission.

Members of Audit and Standards Committee

| | |
|---|--------------------------|
| Councillor Nigel Studdert-Kennedy (Chair) | Councillor Keith Pearson |
| Councillor Rachel Curley (Vice Chair) | Councillor Mark Reeves |
| Councillor Martin Baxendale | Councillor Tom Williams |
| Councillor Stephen Davies | Councillor Penny Wride |
| Councillor Colin Fryer | |

AUDIT AND STANDARDS COMMITTEE

4 July 2017

7.00 pm – 8.55 pm

Council Chamber, Ebley Mill, Stroud

3

Minutes

Membership

| | | | |
|---|---|--------------------------|---|
| Councillor Nigel Studdert-Kennedy (Chair) | P | Councillor Keith Pearson | P |
| Councillor Rachel Curley (Vice-Chair) | P | Councillor Mark Reeves | P |
| Councillor Martin Baxendale | P | Councillor Tom Williams | A |
| Councillor Stephen Davies | A | Councillor Penny Wride | P |
| Councillor Colin Fryer | P | | |

A = Absent P = Present

Officers in attendance

Head of Audit Risk Assurance
Principal Accountant

Principal Procurement Officer
Democratic Services Officer

Also present

Matthew Arthur, KPMG

AC.001

APOLOGIES

Apologies for absence had been received from Councillors Stephen Davies and Tom Williams.

AC.002

DECLARATIONS OF INTEREST

There were none.

AC.003

MINUTES

RESOLVED

That the Minutes of the meeting held on 11 April 2017, are approved as a correct record.

AC.004

PUBLIC QUESTION TIME

There were none.

AC.005 **WORK PROGRAMME**

A meeting had been scheduled to discuss the work programme. It was agreed to add an item to November's meeting on the Multi Services Contract.

RESOLVED **To update the work programme and add the Multi Services Contract to November Committee.**

AC.006 **PROCUREMENT REVIEW**

The Principal Procurement Officer outlined the above report and answered members' questions which covered:-

- The Council's open process for procurement through the portal.
- Obtaining best value when employing agency staff for temporary periods and consultants to bridge the gap in expertise.
- The management of contracts was clearly set out within the procedures and any concerns were highlighted at quarterly meetings held with Corporate Team.

RECOMMEND TO COUNCIL **The thresholds in the Contract and Procurement Procedure Rules be amended as outlined in the Report at paragraphs 2.3 and 2.4.**

AC.007 **ANNUAL REPORT ON INTERNAL AUDIT ACTIVITY 2016/17**

The Head of Audit Risk Assurance (Chief Internal Auditor) highlighted various paragraphs within the above report.

In relation to BACS Direct Debit Internal Audit, concern was expressed that the Business Continuity Plan had not been developed or implemented, putting the Council at potential risk. A Members' Information Sheet would be published which would provide an update on actions currently being taken to address these concerns.

RESOLVED

- a) **Assess, from the findings set out in this Internal Audit Annual Report, that it can take reasonable assurance that the internal control environment, comprising risk management, control and governance is operating effectively;**
- b) **Request senior management attendance at the next meeting of the Committee to provide an update on the actions taken in relation to the recommendations made in the ICT Business Processes limited assurance report; and**
- c) **Note that the performance of Internal Audit meets the required standards.**

AC.008 **DRAFT ANNUAL GOVERNANCE STATEMENT (AGS)**
2016/17

The Head of Audit Risk Assurance (Chief Internal Auditor) outlined the above report, highlighting key paragraphs.

RESOLVED **That the AGS 2016/17 (including the actions planned by the Council to further enhance good governance arrangements), as set out in Appendix A, be approved.**

AC.009 **STATEMENT OF ACCOUNTS 2016/17**

The Principal Accountant presented the above report and answered members' questions including one regarding the value of the Councils' assets.

RESOLVED **To approve the report and considers any recommendations that it would like to make regarding the accounts for the year ending 31 March 2017.**

AC.010 **ANNUAL REPORT ON TREASURY MANAGEMENT**
ACTIVITY AND ACTUAL PRUDENTIAL INDICATORS
2016/2017

In presenting the above report, the Principal Accountant drew attention to several paragraphs. In reply to members' questions he confirmed that the Council were in daily contact with brokers and would obtain the best financial return, within the risk parameters set in the Treasury Strategy.

RESOLVED **To approve the treasury management activity annual report for 2016/2017 and the actual Prudential Indicators.**

AC.011 **MEMBER QUESTIONS**

There were none.

The meeting closed at 8.55 pm.

Chair

STROUD DISTRICT COUNCIL
AUDIT AND STANDARDS COMMITTEE

**AGENDA
ITEM NO**

12 SEPTEMBER 2017

WORK PROGRAMME

5

| Proposed Meeting Date | Report Description | Responsible Officer / Member |
|------------------------------|--|--|
| 28.11.2017 | Partnership Update | Section 151 Officer / Chief Internal Auditor |
| | Annual Audit Letter | KPMG |
| | Multi Services Contract | Public Space Manager |
| | Internal Audit Activity Progress Report 2017/18 | Chief Internal Auditor |
| | Treasury Management Half Year Review | Principal Accountant |
| | Review of Audit Risk Assurance Shared Service | Chief Internal Auditor |
| 06.02.2018 | Annual Summary of Certification of Grant Claims and Returns 2016/17 | KPMG |
| | Annual Governance Statement 2016/17 Improvement Plan | Chief Internal Auditor |
| | Treasury Management Activity 2017/18 | Principal Accountant |
| | Treasury Management, Annual Investment, and MRP Strategy 2018/19 | Principal Accountant |
| | Internal Audit Activity Progress Report 2017/18 | Chief Internal Auditor |
| 10.04.2018 | External Audit Plan 2017/18 | KPMG |
| | Internal Audit Activity Progress Report 2017/18 | Chief Internal Auditor |
| | Internal Audit Plan 2018/19 | Chief Internal Auditor |
| | Annual Report of the Audit and Standards Committee (prepared by the Chairman) for agreement prior to presentation to Council | Chair |

Information sheets relevant to the Committee

| Date sent & (Ref No) | Topic |
|------------------------------------|---|
| 1 June 2017 SR-2017/18-001 | ICT Infrastructure Investment Plan 2017/18 to 2019/20 |
| 1 September 2017 AS-2017/18-001 | Standards Update |
| Pending | Review of Risk Management Framework |



External audit report 2016/17

Stroud District Council

—
31 August 2017

Summary for Audit & Standards Committee

Financial statements This document summarises the key findings in relation to our 2016-17 external audit at Stroud District Council ('the Authority'). This report focusses on our on-site work which was completed in July 2017 on the Authority's significant risk areas, as well as other areas of your financial statements. Our findings are summarised on pages 4 – 14.

Our report also includes additional findings in respect of our control work which we have identified.

Subject to all outstanding queries being resolved to our satisfaction we anticipate issuing an unqualified audit opinion on the Authority's financial statements before the deadline of 30 September.

We have identified one audit adjustment relating to the valuation of housing stock, which was overstated by £7.7 million as a result of a change in the index being applied to revalue this stock subsequent to the draft accounts being prepared. This has been adjusted by management in the final set of financial statement. See page 10 for details.

Based on our work, we have raised one recommendation. Details on our recommendations can be found in Appendix 1.

We are now in the completion stage of the audit.

Use of resources We have completed our risk-based work to consider whether in all significant respects the Authority has proper arrangements to ensure has taken properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people. We have concluded that the Authority has made proper arrangements to secure economy, efficiency and effectiveness in its use of resources.

We therefore anticipate issuing an unqualified value for money opinion.

See further details on page 15-20.

Acknowledgements We would like to take this opportunity to thank officers and Members for their continuing help and co-operation throughout our audit work.

We ask the Audit & Standards Committee to note this report.

Contents

The key contacts in relation to our audit are:

Darren Gilbert

Director

KPMG LLP (UK)

+44 2920 468205

darren.gilbert@kpmg.co.uk

Matthew Arthur

Senior Manager

KPMG LLP (UK)

+44 2920 468006

matthew.arthur@kpmg.co.uk

Ming Hui Ng

Audit in charge

KPMG LLP (UK)

+44 117 905 4672

MingHui.Ng@kpmg.co.uk

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28 5. Audit and non-audit fees

This report is addressed to Stroud District Council (the Authority) and has been prepared for the sole use of the Authority. We take no responsibility to any member of staff acting in their individual capacities, or to third parties. Public Sector Audit Appointments issued a document entitled Statement of Responsibilities of Auditors and Audited Bodies summarising where the responsibilities of auditors begin and end and what is expected from audited bodies. We draw your attention to this document which is available on Public Sector Audit Appointment's website (www.psaa.co.uk).

External auditors do not act as a substitute for the audited body's own responsibility for putting in place proper arrangements to ensure that public business is conducted in accordance with the law and proper standards, and that public money is safeguarded and properly accounted for, and used economically, efficiently and effectively.

We are committed to providing you with a high quality service. If you have any concerns or are dissatisfied with any part of KPMG's work, in the first instance you should contact Darren Gilbert, the engagement lead to the Authority, who will try to resolve your complaint. If you are dissatisfied with your response please contact the national lead partner for all of KPMG's work under our contract with Public Sector Audit Appointments Limited, Andrew Sayers (on 0207 694 8981, or by email to andrew.sayers@kpmg.co.uk). After this, if you are still dissatisfied with how your complaint has been handled you can access PSAA's complaints procedure by emailing generalenquiries@psaa.co.uk, by telephoning 020 7072 7445 or by writing to Public Sector Audit Appointments Limited, 3rd Floor, One, Smith Square, London, SW1P 3H.

Section one

Financial Statements



We anticipate issuing an unqualified audit opinion on the Authority's 2016/17 financial statements by 30 September 2017. We will also report that your Annual Governance Statement complies with the guidance issued by CIPFA/SOLACE (*'Delivering Good Governance in Local Government'*) published in April 2016.

For the year ending 31 March 2017, the Authority has reported a surplus of £33.8m. The impact on reserves after statutory accounting adjustments has been a decrease in the General Fund of £0.9m and an increase in the HRA account of £4.2m.



Significant audit risks

Our *External Audit Plan 2016/17* sets out our assessment of the Authority's significant audit risks. We have completed our testing in these areas and set out our evaluation following our work:

| Significant audit risks | Work performed |
|---|--|
| 1. Significant changes in the pension liability due to LGPS Triennial Valuation. | <p data-bbox="445 547 651 573">Why is this a risk?</p> <p data-bbox="445 592 1322 762">During the year, the Local Government Pension Scheme which is administered by Gloucestershire County Council (the Pension Fund) has undergone a triennial valuation with an effective date of 31 March 2016 in line with the Local Government Pension Scheme (Administration) Regulations 2013. The Authority's share of pensions assets and liabilities is determined in detail, and a large volume of data is provided to the actuary in order to carry out this triennial valuation.</p> <p data-bbox="445 793 1348 903">The pension liability numbers to be included in the financial statements for 2016/17 are based on the output of the triennial valuation rolled forward to 31 March 2017. For 2017/18 and 2018/19 the actuary will then roll forward the valuation for accounting purposes based on more limited data.</p> <p data-bbox="445 934 1336 1044">There is a risk that the data provided to the actuary for the valuation exercise is inaccurate and that these inaccuracies affect the actuarial figures in the accounts. Most of the data is provided to the actuary by Gloucestershire County Council, which administers the Pension Fund.</p> <p data-bbox="445 1079 776 1106">Our work to address this risk</p> <p data-bbox="445 1125 1333 1234">Further to the usual procedures over pension balances, we have agreed data provided by the Authority to the actuary relating to the triennial valuation, back to the relevant systems and reports from which it was derived, in addition to checking the accuracy of this data.</p> <p data-bbox="445 1265 1336 1348">We have also liaised with Grant Thornton, who are the auditors of the Pension Fund, where this data was provided by the Pension Fund on the Authority's behalf to check the completeness and accuracy of such data.</p> |

Considerations required by professional standards

Fraud risk of revenue recognition

Professional standards require us to make a rebuttable presumption that the fraud risk from revenue recognition is a significant risk.

In our *External Audit Plan 2016/17* we reported that we do not consider this to be a significant risk for Local Authorities as there is unlikely to be an incentive to fraudulently recognise revenue.

This is still the case. Since we have rebutted this presumed risk, there has been no impact on our audit work.



Management override of controls

Professional standards require us to communicate the fraud risk from management override of controls as significant because management is typically in a unique position to perpetrate fraud because of its ability to manipulate accounting records and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively.

Our audit methodology incorporates the risk of management override as a default significant risk. We have not identified any specific additional risks of management override relating to this audit.

In line with our methodology, we carried out appropriate controls testing and substantive procedures, including over journal entries, accounting estimates and significant transactions that are outside the normal course of business, or are otherwise unusual.

There are no matters arising from this work that we need to bring to your attention.

Other areas of audit focus

We identified two areas of audit focus. These are not considered as significant risks as they are less likely to give rise to a material error. Nonetheless these are areas of importance where we would carry out substantive audit procedures to ensure that there is no risk of material misstatement.

| Other areas of audit focus | Our work to address the areas |
|----------------------------|-------------------------------|
|----------------------------|-------------------------------|

| | |
|---|-------------------|
| 1. Disclosures associated with retrospective restatement of CIES, EFA and MiRS | Background |
|---|-------------------|

CIPFA has been working with stakeholders to develop better accountability through the financial statements as part of its 'telling the whole story' project. The key objective of this project was to make Local Government accounts more understandable and transparent to the reader in terms of how councils are funded and how they use the funding to serve the local population. The outcome of this project has resulted in two main changes in respect of the 2016-17 Local Government Accounting Code (the Code) as follows:

- Allowing local authorities to report on the same basis as they are organised by removing the requirement for the Service Reporting Code of Practice (SeRCOP) to be applied to the Comprehensive Income and Expenditure Statement (CIES); and
- Introducing an Expenditure and Funding Analysis (EFA) which provides a direct reconciliation between the way local authorities are funded and prepare their budget and the CIES. This analysis is supported by a streamlined Movement in Reserves Statement (MIRS) and replaces the current segmental reporting note.

As a result of these changes, retrospective restatement of the CIES (cost of services), EFA and MIRS is required from 1 April 2016 in the Statement of Accounts. The new disclosure requirements and the restatement of the accounts require compliance with relevant guidance and the correct application of applicable Accounting Standards. This is therefore an important material disclosure change in this year's accounts, worthy of audit understanding.

What we have done

We have liaised with the Authority's finance team regarding the new requirements and have agreed the new disclosures, including the restatement of the prior year comparators, to supporting documentation including financial information reported to Members.

| | |
|----------------------------------|-------------------|
| 2. Fair Value of Property | Background |
|----------------------------------|-------------------|

The Council holds a significant property portfolio and needs to consider whether the carrying value of property assets is materially stated as at the balance sheet date. In doing so, it should pay particular consideration to complex development schemes or property earmarked for a change in usage or as surplus to ensure the valuation of these as per the most recent valuation is still appropriate.

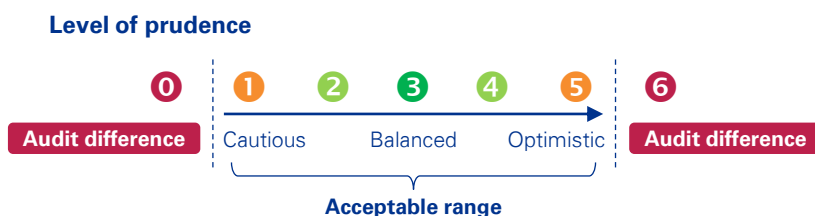
What we have done

We reviewed the appropriateness of the valuation methodology and considered the expertise of the valuer performing the exercise. We have also reviewed the Council's consideration of the accuracy of the year-end carrying value of properties not revalued at balance sheet date. Testing was performed on a sample of property revaluation and discussions were held with management to gain an understanding of the changes in use/surplus properties and how these have been considered in the valuations.

As a result of our work, an audit adjustment of £7.7m was raised in relation to changes in the housing index applied by the Council subsequent to the accounts being prepared. This adjustment has been corrected by management (see page 10 and Appendix 2).

Judgements

We have considered the level of prudence within key judgements in your 2016/17 financial statements and accounting estimates. We have set out our view below across the following range of judgements.



| Subjective areas | 2016/17 | 2015/16 | Commentary |
|---|---------|---------|---|
| Provisions | 3 | 3 | <p>The amount of provisions is immaterial and in line with prior year balance. The balance mainly includes a provision for NNDR appeals. We consider the provision disclosures to be proportionate.</p> <p>Current Year: £0.7m Prior Year: £0.7m</p> |
| Property, Plant and Equipment (valuations/asset lives) | 4 | 3 | <p>Property, plant and equipment is made up of £256m council dwellings, £51m other land and buildings, and £5.9m non-property assets. The property assets are depreciated over their useful lives and valued over a five year period. An in-house valuer assesses 20% of the non-housing assets each year across each property class, with housing assets being revalued on an index basis every year with a more detailed “beacon” valuation every 5 years. We reviewed a sample of revalued assets and noted that these were accounted for correctly.</p> <p>An audit adjustment was raised in relation to changes in the housing index applied by the Council subsequent to the accounts being prepared. This adjustment has been corrected by management (see page 10 and Appendix 2).</p> <p>We consider that the valuation approach for this year is sufficient to avoid the risk of a material audit difference in the assets which have not been revalued, but the Council should remain alert to the potential of material movements in non-revalued asset values in future years.</p> |
| Pensions | 3 | 3 | <p>Assumptions are set when calculating the liability amount. The key assumptions used by the actuary were reviewed and appear reasonable for the purpose of IAS19.</p> |

Proposed opinion and audit differences

Subject to all outstanding queries being resolved to our satisfaction, we anticipate issuing an unqualified audit opinion on the Authority's 2016/17 financial statements following approval of the Statement of Accounts by the Audit & Standards Committee on 12 September 2017.

Audit differences

In accordance with ISA 260 we are required to report uncorrected audit differences to you. We also report any material misstatements which have been corrected and which we believe should be communicated to you to help you meet your governance responsibilities.

The final materiality level for this year's audit was set at £1.5 million (see Appendix 4). Audit differences below £1.1 million are not considered significant.

Our audit identified a total of one significant audit difference, which we set out in Appendix 2. It is our understanding that this will be adjusted in the final version of the financial statements.

The tables on the right illustrate the total impact of audit differences on the Authority's movements on the General Fund and HRA for the year and balance sheet as at 31 March 2017. The tables also include changes arising from management's identification for reclassification of figures.

There is no net impact on the General Fund and HRA balances as at 31 March 2017 as a result of audit adjustments. However, there is a £7.7m reduction to the value of Property, Plant and Equipment and an increase in downwards revaluation through the HRA I&E of £2.5m as a result of the housing stock valuation error noted on pages 8 and 9, and summarised in Appendix 2.

In addition, we identified a number of presentational adjustments required to ensure that the accounts are compliant with the Code of Practice on Local Authority Accounting in the United Kingdom 2016/17 ('the Code'). The Authority has addressed these where significant.

| Movements on the general and HRA fund 2016/17 | | | |
|--|--------------|--------------|------------------|
| £'000 | Pre-audit | Post-audit | Ref ¹ |
| Surplus on the provision of services | 36,303 | 33,825 | 1 |
| Adjustments between accounting basis and funding basis under Regulations (GR and HRA only) | -32,999 | -30,521 | |
| Increase in General Fund and HRA (including earmarked reserves) | 3,304 | 3,304 | |

| Balance sheet as at 31 March 2017 | | | |
|-----------------------------------|----------------|----------------|------------------|
| £'000 | Pre-audit | Post-audit | Ref ¹ |
| Property, plant and equipment | 320,059 | 312,401 | 1 |
| Other long term assets | 2,947 | 2,947 | |
| Current assets | 38,264 | 38,404 | |
| Current liabilities | -10,883 | -10,883 | |
| Long term liabilities | -154,718 | -154,858 | |
| Net worth | 195,670 | 188,012 | |
| General Fund | 2,169 | 2,169 | |
| Other usable reserves | 26,495 | 26,495 | |
| Unusable reserves | 167,006 | 159,348 | 1 |
| Total reserves | 195,670 | 188,012 | |

¹ See referenced adjustments in Appendix 2.

Section one: financial statements

Annual governance statement

We have reviewed the Authority's 2016/17 Annual Governance Statement and confirmed that:

- It complies with *Delivering Good Governance in Local Government: A Framework* published by CIPFA/SOLACE; and
- It is not misleading or inconsistent with other information we are aware of from our audit of the financial statements.

We have made a small number of comments in respect of its format and content which the Authority has agreed to amend where significant.

Subsequent to the draft accounts, the Council has made a decision to publish the Annual government statement as a separate document to the Statement of Accounts and display together on the website in line with CIPFA recommendations.

Narrative report

We have reviewed the Authority's 2016/17 narrative report and have confirmed that it is consistent with the financial statements and our understanding of the Authority.

Accounts production and audit process

Our audit standards (*ISA 260*) require us to communicate our views on the significant qualitative aspects of the Authority's accounting practices and financial reporting.

We also assessed the Authority's process for preparing the accounts and its support for an efficient audit. The efficient production of the financial statements and good-quality working papers are critical to meeting the tighter deadlines.

KPMG Central

The Authority continues to use our KPMG Central tool. KPMG Central has allowed the team to securely transfer large amounts of data between the Authority and the audit team. KPMG Central aligns to our Accounts Audit Protocol and allows the Authority's Closedown Team to efficiently share requested information. Feedback from the finance team continues to be positive.

Accounting practices and financial reporting

The Authority has recognised the additional pressures which the earlier closedown in 2017/18 will bring. We have been engaging with the Authority in the period leading up to the year end in order to proactively address issues as they emerge.

The Authority has finalising the accounts in a shorter timescale which puts the Authority in a good position to meet the new 2017/18 deadline. Nonetheless, there is scope to improve the process further by putting in place additional reviews of working papers and sharing audit responsibility (see sections below) to make sure the 2017/18 audit deadline is achieved.

We consider the Authority's accounting practices appropriate.

Completeness of draft accounts

We received a complete set of draft accounts in advance of the 30 June statutory deadline.

Quality of supporting working papers

We issued our *Accounts Audit Protocol 2016/17* ("Prepared by Client" request) which outlines our documentation request. This helps the Authority [and the Fund] to provide audit evidence in line with our expectations.

While the quality of working papers were generally good quality, we did identify some issues in relation to certain working papers (e.g. capital supporting papers not reconciling to accounts note) which resulted in some delays in auditor understanding and increased auditor queries. This may be as a result of faster closing timelines.

There is an opportunity for improvements to be made in providing clear and concise audit trail of underlying transactions.



Response to audit queries

Officers generally dealt with our audit queries swiftly although we experienced some delays in certain areas, in particular queries where the query was redirected to multiple individuals.

There is still room for improvement in this area, in particular to ensure there is sufficient audit responsibility spread around the finance team to avoid delays due to requests building up with key individuals from multiple auditors, which are a risk when the deadlines are shortened and our audit visit will require more staff over a shorter period.

Prior year recommendations

As part of our audit we have specifically followed up the Authority's progress in addressing the recommendations in last year's ISA 260 report.

The Authority has not yet implemented the recommendation in our ISA 260 Report 2015/16.

Appendix 1 provides further details.

Controls over key financial systems

We have tested controls as part of our focus on significant audit risks and other parts of your key financial systems on which we rely as part of our audit. The strength of the control framework informs the substantive testing we complete during our final accounts visit.

Based on the work performed, we are satisfied that the controls relating to our audit approach are performing effectively. We are able to place reliance on these controls where planned.

Collection fund balances

In previous years we have included a comment in our report in relation to the deficit on the business rates element of the Collection Fund.

This deficit continues to decrease following a surplus of £823,000 this year and is now down to £70k as at 31 March 2017.

The Council Tax element of the fund has made a deficit of £51k this year but remains in credit overall of £1,136k.

As in previous years, the Authority is applying established processes to recover the deficit in future years. No issues have been identified in our review of the accounting of either part of the fund.

Completion

We confirm that we have complied with requirements on objectivity and independence in relation to this year's audit of the Authority's 2016/17 financial statements.

Before we can issue our opinion we require a signed management representation letter.

Once we have finalised our opinions and conclusions we will prepare our Annual Audit Letter and close our audit.

Declaration of independence and objectivity

As part of the finalisation process we are required to provide you with representations concerning our independence.

In relation to the audit of the financial statements of Stroud District Council ending 31 March 2017, we confirm that there were no relationships between KPMG LLP and Stroud District Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

We have provided a detailed declaration in Appendix 4 in accordance with ISA 260.

Management representations

You are required to provide us with representations on specific matters such as your financial standing and whether the transactions within the accounts are legal and unaffected by fraud. We have provided a template to the s151 Officer for presentation to the Audit & Standards Committee. We require a signed copy of your management representations before we issue our audit opinion.

Other matters

ISA 260 requires us to communicate to you by exception 'audit matters of governance interest that arise from the audit of the financial statements' which include:

- Significant difficulties encountered during the audit;
- Significant matters arising from the audit that were discussed, or subject to correspondence with management;
- Other matters, if arising from the audit that, in the auditor's professional judgment, are significant to the oversight of the financial reporting process; and

- Matters specifically required by other auditing standards to be communicated to those charged with governance (e.g. significant deficiencies in internal control; issues relating to fraud, compliance with laws and regulations, subsequent events, non disclosure, related party, public interest reporting, questions/objections, opening balances etc.).

There are no other matters which we wish to draw to your attention in addition to those highlighted in this report.



Section two

Value for money

Our 2016/17 VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We have concluded that the Authority has made proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

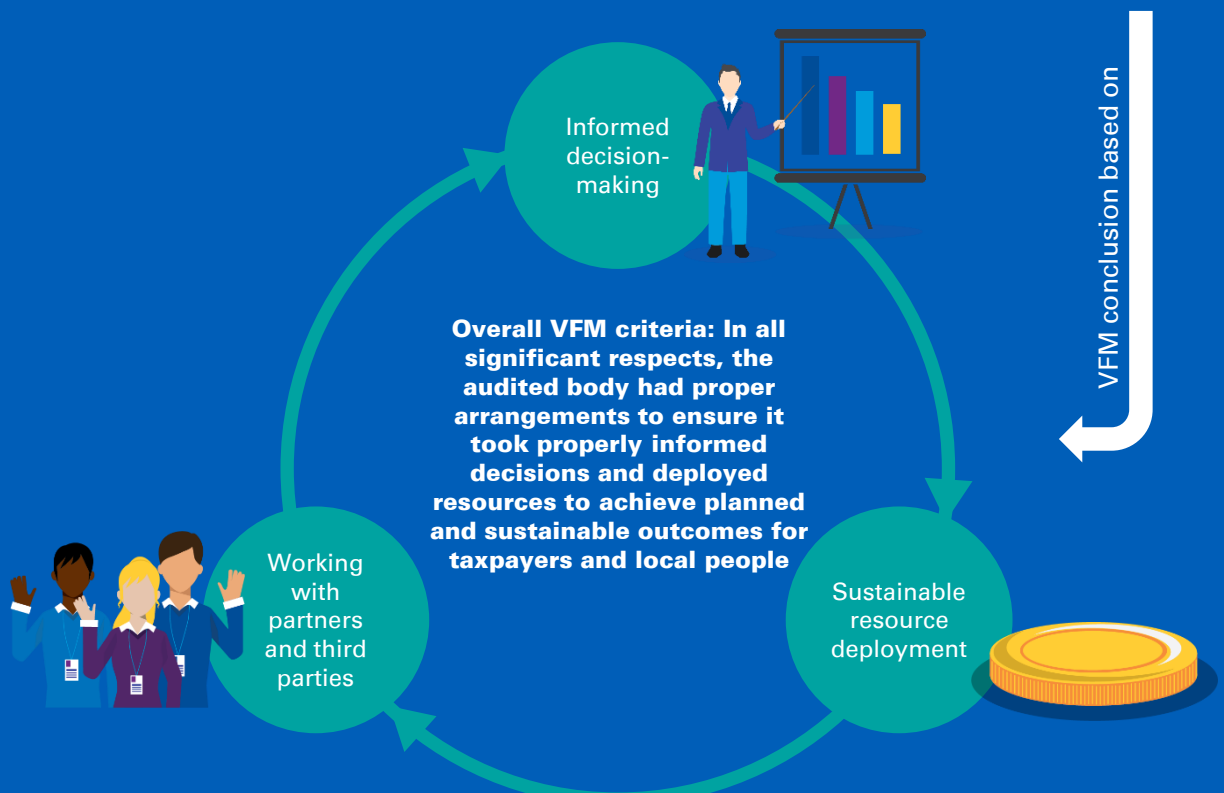
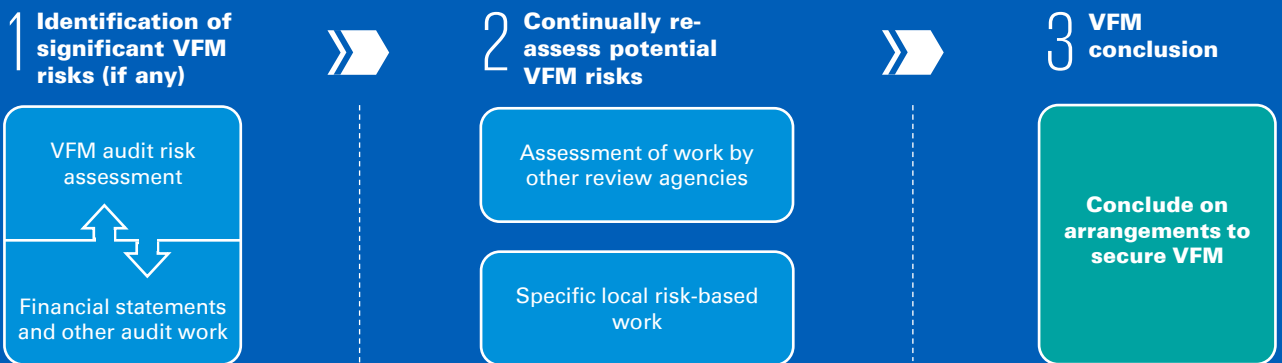
VFM conclusion

The Local Audit and Accountability Act 2014 requires auditors of local government bodies to be satisfied that the authority ‘has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources’.

This is supported by the Code of Audit Practice, published by the NAO in April 2015, which requires auditors to ‘take into account their knowledge of the relevant local sector as a whole, and the audited body specifically, to identify any risks that, in the auditor’s judgement, have the potential to cause the auditor to reach an inappropriate conclusion on the audited body’s arrangements.’

Our VFM conclusion considers whether the Authority had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

We follow a risk based approach to target audit effort on the areas of greatest audit risk.



The table below summarises our assessment of the individual VFM risks identified against the three sub-criteria. This directly feeds into the overall VFM criteria and our value for money opinion.

| VFM assessment summary | | | |
|--|---------------------------------|--|--|
| VFM risk | Informed decision-making | Sustainable resource deployment | Working with partners and third parties |
| 1. Financial Resilience in the local and national Economy | ✓ | ✓ | ✓ |
| 2. Contract Procurement | ✓ | ✓ | ✓ |
| Overall summary | ✓ | ✓ | ✓ |

In consideration of the above, we have concluded that in 2016/17, the Authority has made proper arrangements to ensure it took properly-informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

In line with the risk-based approach set out on the previous page, we have:

- assessed the Authority’s key business risks which are relevant to our VFM conclusion;
- identified the residual audit risks for our VFM conclusion, taking account of work undertaken in previous years or as part of our financial statements audit;
- considered the results of relevant work by the Authority, inspectorates and review agencies in relation to these risk areas; and
- completed specific local risk based work.

Further details on the work done and our assessment are provided on the following pages.

Significant VFM risks

We have identified two significant VFM risks, as communicated to you in our *2016/17 External Audit Plan*. In all cases we are satisfied that external or internal scrutiny provides sufficient assurance that the Authority’s current arrangements in relation to these risk areas are adequate.

| Significant VFM risks | Work performed |
|--|---|
| <p>1. Achievement of the Savings Plan</p> | <p>Why is this a risk?</p> <p>There has been a significant shift in the national outlook over the last 12 months, primarily driven by the outcome of the referendum on 23 June 2016 on the UK’s membership of the European Union. Consequently GDP growth forecasts have been revised downwards, which potentially reduces the level of any growth in business rates income. Inflationary pressures, service pressures, and a reduction in the local government finance settlement will impact on the Authority’s finances.</p> <p>In December 2016, the Authority published a draft Medium Term Financial Plan (MTFP) 2017/18 –2021/22 (which incorporates its Efficiency Plan published in September 2016) that sets out a balanced budget for 2017/18.</p> <p>From 2018/19, the Authority has identified funding gaps; however it is confident that the targets in the Efficiency Plan are sufficient to bridge the forecast gap in the MTFP and are monitored by the management board. The Authority’s proposed new governance arrangements include a specific officer board focussed on the delivery of the Efficiency Plan and associated improvement projects.</p> <p>Summary of our work</p> <p>Like most of local government, the Authority faces a challenging future driven by funding reductions and an increase in demand for services.</p> <p>The Authority reported an overall breakeven position on its net expenditure budget for 2016/17 after the net contribution of £0.36m from the Earmarked General Fund reserve. This enabled the uncommitted General Fund balance to remain at £2.2 million as of 31 March 2017.</p> <p>The Authority’s Medium Term Financial Plan (MTFP) details a balanced budget for 2017/18 after use of reserves of £567,000, including savings of £25,000 in year, all of which have been identified. However, the MTFP details the increasingly difficult financial challenges faced each year, with the current MTFP using reserves of £1.8m in 2018/19, £2.8m in 2019/20 and £341k in 2020/21, after which the general funds are likely to be fully diminished (the 2020/21 budget showing a deficit of £3.3m after use of reserves).</p> <p>However, this is intended as a worst case scenario budget (it includes only £170k of savings) and the Council is actively working on further savings plans to reduce the required reserves usage, as well as investigating potential for increased income generation.</p> <p>Based on our review of the plans in place and understanding of the actions being taken, there are no factors impacting adversely on our VFM conclusion.</p> |

| Significant VFM risks | Work performed |
|-----------------------|--|
| 2. Procurement | <p data-bbox="445 428 1349 540">Why is this a risk?</p> <p data-bbox="445 428 1349 540">In 2014/15 we issued a qualified VFM opinion as a result of instances identified in our and in internal audit's work where the Council had not followed its own procurement policies by failing to operate an appropriate procurement exercise and by making inappropriate variations to existing contracts.</p> <p data-bbox="445 561 1349 727">In 2015/16, our work found that while it was clear that there remained some discrepancies in procurement procedures, the issues were much reduced from last year and less significant in nature. In addition, we did not identify any issues in the most significant new arrangements established during the year. Based on this, we considered that sufficient improvements had been made for us to issue an unqualified VFM conclusion.</p> <p data-bbox="445 747 1349 830">However, it remains important that the Council continues to focus on making improvements to its procurement arrangements, both through the processes in place and the extent to which they are applied in practice.</p> <p data-bbox="445 878 696 905">Summary of our work</p> <p data-bbox="445 926 1349 975">In 2016/17, we reviewed the work of internal audit over procurement and considered if any significant new contracts required additional work.</p> <p data-bbox="445 996 1349 1046">There were no significant issues resulting from internal audit work during the year, and no major contracts let during the year.</p> <p data-bbox="445 1067 1349 1116">In addition, we have reviewed the procurement action plan and confirmed that it is on target.</p> <p data-bbox="445 1137 1349 1166">On this basis, there are no factors impacting adversely on our VFM conclusion.</p> |

A close-up photograph of a stack of books on a wooden surface. The books have various colored covers, including a prominent red one. A silver pen is lying on the wooden surface in the foreground. The background is softly blurred, showing more books and a warm, natural light.

Appendices

Follow-up of prior year recommendations

In the previous year, we raised one recommendation which we reported in our *External Audit Report 2015/16 (ISA 260)*. The Authority has not yet implemented all of the recommendations. We reiterate the importance of the outstanding recommendations and recommend that these are implemented by the Authority.

We have used the same rating system as explained in Appendix 1.

Each recommendation is assessed during our 2016/17 work, and we have obtained the recommendation's status to date. We have also obtained Management's assessment of each outstanding recommendation.

Below is a summary of the prior year's recommendations.

2015/16 recommendations status summary

| Priority | Number raised | Number implemented / superseded | Number outstanding |
|--------------|---------------|---------------------------------|--------------------|
| High | 0 | 0 | 0 |
| Medium | 1 | 0 | 1 |
| Low | 0 | 0 | 0 |
| Total | 1 | 0 | 1 |

Follow-up of prior year recommendations



1. Purchase data analytics findings

We performed a range of analytics over purchase ledger data for 2015/16, which identified a number of areas for follow up by management:

- a significant amount of invoices were raised without purchase order within the Agresso system; and
- a significant amount of purchase orders were raised after the invoice date.

This means there is a risk that the purchase order authorisation control is not operating correctly for these invoices.

In addition, we identified a number of transactions which are possibly duplicate which we have provided to management for follow-up

Recommendation

Management should follow up on the items identified and consider whether process changes or additional training/education is required regarding the use of Purchase Orders.

Management original response

The Council recognises the importance of raising purchase orders (POs) for goods and services within the Agresso system. The processing and payment of invoices has been subject to a 'Systems Thinking' review in the last 12 months.

This review recommended that POs should be raised for all invoices where possible, with some notable exceptions such as utilities and Tenant Services repairs and works orders. It also recommended that the finance team, after a transitional period, should enforce PO compliance so that invoices presented for payment without a valid PO would not be processed and returned to the supplier.

The finance team are currently considering the timing of this change. It is likely that the Agresso system will require a significant upgrade in the coming months. Therefore, it would be more practical to delay the rollout of enforced PO compliance until we have had more time to understand the impact an upgrade would have on the way POs and invoices are processed in Agresso.

Owner

David Stanley

Original deadline

March 2017

KPMG's 2017 assessment

Not implemented

The recommendation has not been implemented during this financial year as management wishes to roll out in line with upgrades to the Agresso system which have not yet taken place.

Management's 2017 response

The Council has agreed to implement a 'No purchase order, no payment' policy following a finance and wider review of the creditor payments process. Implementation has been put on hold until the financial system is upgraded. The Council hoped to undertake this in May-September 2017, but for various reasons this is not expected to take place until May-September 2018.

The Council decided that there is limited benefit to the organisation of introducing a change to the process before the upgrade, given the upgrade itself may change the process.

Audit differences

We are required by ISA 260 to report all uncorrected misstatements, other than those that we believe are clearly trivial, to those charged with governance (which in your case is the Audit & Standards Committee). We are also required to report all material misstatements that have been corrected but that we believe should be communicated to you to assist you in fulfilling your governance responsibilities.

A number of minor amendments focused on presentational improvements have also been made to the 2016/17 draft financial statements. The Finance team is committed to continuous improvement in the quality of the financial statements submitted for audit in future years.

Adjusted audit differences

The following table sets out the significant audit differences identified by our audit of Stroud’s financial statements for the year ended 31 March 2017. These have all been adjusted in the financial statements presented to this committee.

| No. | Income and expenditure statement | Movement in reserves statement | Assets | Liabilities | Reserves | Basis of audit difference |
|-----|---|---|--|-------------|--|---|
| 1 | DR Council Dwelling Revaluation £2,478 | DR adjustment between accounting and funding basis (Capital adjustment account) £2,478 CR adjustment between accounting and funding basis (HRA) £2,478 | CR Property, Plant and Equipment £7,658 | | DR Revaluation Reserve (OCI) £5,180 | Housing stock valuation This relates to a downward adjustment on Property, Plant and Equipment to reflect the most up to date index in the revaluation figure. The adjustment is due to the timing difference arising from when the index was obtained by the Council from the Land Registry Website. A 10.44% Index Factor for December 2016 was used differs when preparing the draft financial statements, but by the time of the audit this had been adjusted down by the Land Registry to 7.15%. This resulted in the value of housing sock being overstated by £7.7m difference and HRA downwards revaluation being understated by £2.5m. |
| | DR £2,478 | 0 | CR £7,658 | | DR £5,180 | |

Unadjusted audit differences

The following table sets out the uncorrected audit differences identified by our audit of Stroud District Council's financial statements for the year ended 31 March 2017. These differences are individually below our materiality level of £1.5 million. Cumulatively, the impact of these uncorrected audit differences is £320,000. We have also considered the cumulative impact of these unadjusted audit differences on the Authority's financial statements in forming our audit opinion.

Table 2: Unadjusted audit differences (£'000)

| No. | Income and expenditure statement | Movement in reserves statement | Assets | Liabilities | Reserves | Basis of audit difference |
|-----|----------------------------------|---|-----------------------------|-----------------------|----------|---|
| 1 | | Cr General fund £320,000 Dr Pension Reserve £320,000 | Cr Pensions Assets £320,000 | Dr Creditors £320,000 | | This relates to March 2017 pension contributions which had not been paid to the pension administrator (Gloucestershire County Council) prior to year end. International Accounting Standard (IAS) 19 Employee Benefits specifically stipulates that unpaid contributions cannot be considered as part of the plan assets as they are a non-transferable asset until they are paid over. The impact of this misstatement is only on the balance sheet and on the mechanics of the pension transactions within the accounts, as the Council has an equivalent creditor balance to the pension scheme. |
| | - | - | Cr £320,000 | Dr £320,000 | - | |

Materiality and reporting of audit differences

The assessment of what is material is a matter of professional judgment and includes consideration of three aspects: materiality by value, nature and context.

Material errors by value are those which are simply of significant numerical size to distort the reader's perception of the financial statements. Our assessment of the threshold for this depends upon the size of key figures in the financial statements, as well as other factors such as the level of public interest in the financial statements.

Errors which are material by nature may not be large in value, but may concern accounting disclosures of key importance and sensitivity, for example the salaries of senior staff.

Errors that are material by context are those that would alter key figures in the financial statements from one result to another – for example, errors that change successful performance against a target to failure.

We used the same planning materiality reported in our External Audit Plan 2016/17, presented to you in March 2017.

Materiality for the Authority's accounts was set at £1.5million which equates to around 2 percent of gross expenditure. We design our procedures to detect errors in specific accounts at a lower level of precision.

Reporting to the Audit & Standards Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit & Standards Committee of lesser amounts to the extent that these are identified by our audit work.

Under *ISA 260*, we are obliged to report omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. *ISA 260* defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria.

ISA 450 requires us to request that uncorrected misstatements are corrected.

In the context of the Authority, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £75,000 for the Authority.

Where management have corrected material misstatements identified during the course of the audit, we will consider whether those corrections should be communicated to the Audit & Standards Committee to assist it in fulfilling its governance responsibilities.

Declaration of independence and objectivity

Auditors appointed by Public Sector Audit Appointments Ltd must comply with the Code of Audit Practice (the 'Code') which states that:

"The auditor should carry out their work with integrity, objectivity and independence, and in accordance with the ethical framework applicable to auditors, including the ethical standards for auditors set by the Financial Reporting Council, and any additional requirements set out by the auditor's recognised supervisory body, or any other body charged with oversight of the auditor's independence. The auditor should be, and should be seen to be, impartial and independent. Accordingly, the auditor should not carry out any other work for an audited body if that work would impair their independence in carrying out any of their statutory duties, or might reasonably be perceived as doing so."

In considering issues of independence and objectivity we consider relevant professional, regulatory and legal requirements and guidance, including the provisions of the Code, the detailed provisions of the Statement of Independence included within the Public Sector Audit Appointments Ltd Terms of Appointment ('Public Sector Audit Appointments Ltd Guidance') and the requirements of APB Ethical Standard 1 Integrity, Objectivity and Independence ('Ethical Standards').

The Code states that, in carrying out their audit of the financial statements, auditors should comply with auditing standards currently in force, and as may be amended from time to time. Public Sector Audit Appointments Ltd guidance requires appointed auditors to follow the provisions of *ISA (UK&I) 260 'Communication of Audit Matters with Those Charged with Governance'* that are applicable to the audit of listed companies. This means that the appointed auditor must disclose in writing:

- Details of all relationships between the auditor and the client, its directors and senior management and its affiliates, including all services provided by the audit firm and its network to the client, its directors and senior management and its affiliates, that the auditor considers may reasonably be thought to bear on the auditor's objectivity and independence.
- The related safeguards that are in place.
- The total amount of fees that the auditor and the auditor's network firms have charged to the client and its affiliates for the provision of services during the reporting period, analysed into appropriate categories, for example, statutory audit services, further audit services, tax advisory services and other non-audit services. For each category, the amounts of any future services which have been contracted or where a written proposal has been submitted are separately disclosed. We do this in our Annual Audit Letter.

Appointed auditors are also required to confirm in writing that they have complied with Ethical Standards and that, in the auditor's professional judgement, the auditor is independent and the auditor's objectivity is not compromised, or otherwise declare that the auditor has concerns that the auditor's objectivity and independence may be compromised and explaining the actions which necessarily follow from this. These matters should be discussed with the Audit & Standards Committee.

Ethical Standards require us to communicate to those charged with governance in writing at least annually all significant facts and matters, including those related to the provision of non-audit services and the safeguards put in place that, in our professional judgement, may reasonably be thought to bear on our independence and the objectivity of the Engagement Lead and the audit team.

General procedures to safeguard independence and objectivity

KPMG LLP is committed to being and being seen to be independent. As part of our ethics and independence policies, all KPMG LLP Audit Partners and staff annually confirm their compliance with our Ethics and Independence Manual including in particular that they have no prohibited shareholdings.

Our Ethics and Independence Manual is fully consistent with the requirements of the Ethical Standards issued by the UK Auditing Practices Board. As a result we have underlying safeguards in place to maintain independence through: Instilling professional values, Communications, Internal accountability, Risk management and Independent reviews.

We would be happy to discuss any of these aspects of our procedures in more detail.

Auditor declaration

In relation to the audit of the financial statements of Stroud District Council for the financial year ending 31 March 2017, we confirm that there were no relationships between KPMG LLP and Stroud District Council, its directors and senior management and its affiliates that we consider may reasonably be thought to bear on the objectivity and independence of the audit engagement lead and audit staff. We also confirm that we have complied with Ethical Standards and the Public Sector Audit Appointments Ltd requirements in relation to independence and objectivity.

Audit and non-audit fees

Audit fees

As communicated to you in our External Audit Plan 2016/17, our scale fee for the audit is £51,975 plus VAT, which is the same as prior year.

Non-audit work and independence

Below we have listed the non-audit work performed and set out how we have considered and mitigated (where necessary) potential threats to our independence.

| Summary of non-audit work | | |
|--|----------------|--|
| Description of non-audit service | Estimated fee | Potential threat to auditor independence and associated safeguards in place |
| Certification of Housing Benefit Claim | £7,590 | <p>Self-interest: The audit fee scale rates were set independently to KPMG by the PSAA and are not material to the audit fee. Therefore, the proposed engagement will have no perceived or actual impact on the audit team and the audit team resources that will be deployed to perform a robust and thorough audit.</p> <p>Self-review: The work is to provide a certification and does not provide any accounting decisions or advice that would require as part of the financial statements audit.</p> <p>Management threat: No decisions or advice to be provided as part of this work, as it is an audit related certification.</p> <p>Familiarity: This threat is limited given the scale, nature and timing of the work.</p> <p>Advocacy: We will not act as advocates for the Authority in any aspect of this work.</p> <p>Intimidation: not applicable</p> |
| Agreed upon procedures over HCA Social Housing Assistance and grants | £2,000 | <p>Self-interest: Both these engagements are outside the PSAA regime and have fees set by KPMG but which are not material to the audit fee. Therefore, the proposed engagement will have no perceived or actual impact on the audit team and the audit team resources that will be deployed to perform a robust and thorough audit. The HCA procedures also have a different engagement partner.</p> <p>Self-review: The work is to provide a certification or results of procedures and do not provide any accounting decisions or advice that would require as part of the financial statements audit.</p> <p>Management threat: No decisions or advice to be provided as part of this work, as it is an audit related certification.</p> <p>Familiarity: This threat is limited given the scale, nature and timing of the work.</p> <p>Advocacy: We will not act as advocates for the Authority in any aspect of this work.</p> <p>Intimidation: not applicable</p> |
| Certification of Pooling of Housing Capital Receipts Return | £3,500 | |
| Total estimated fees | £13,090 | |
| Total estimated fees as a percentage of the external audit fees | 25% | |



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STROUD DISTRICT COUNCIL
AUDIT AND STANDARDS COMMITTEE

**AGENDA
ITEM NO**

12 SEPTEMBER 2017

7

| | |
|---|---|
| Report Title | STATEMENT OF ACCOUNTS 2016/17 |
| Purpose of Report | To approve the Statement of Accounts 2016/17 and receive KPMG's audit opinion, including the changes to the accounts since the unaudited accounts were signed off by the Section 151 Officer on 16 June 2017. |
| Decision(s) | Committee RESOLVES to approve the audited Statement of Accounts for the year ending 31 March 2017. |
| Consultation and Feedback | Not applicable. |
| Financial Implications and Risk Assessment | There are no financial implications arising directly from this report. David Stanley, Accountancy Manager (S151 Officer) Tel: 01453 754100 Email: david.stanley@stroud.gov.uk |
| Legal Implications | The recommendation and the report details are consistent with legal requirements regarding approval of annual accounts. K Trickey, Legal Services Manager Email: karen.trickey@stroud.gov.uk |
| Report Author | Graham Bailey, Principal Accountant Tel: 01453 754133 Email: graham.bailey@stroud.gov.uk |
| Options | None. |
| Performance Management Follow Up | Actions arising from KPMG's ISA 260 report. |
| Background Papers/ Appendices | Appendix A – Statement of Accounts 2016/17 |

Discussion

1. In accordance with requirements under the Accounts and Audit Regulations 2015, the Accountancy Manager (Section 151 Officer) is required to sign and date the Statement of Accounts by 30 June and certify that it presents a true and fair view of the financial position of the Council at the end of March 2017 and its income and expenditure.
2. The Statement of Accounts for 2016/17 was signed as approved by the Accountancy Manager (Section 151 Officer) on 16 June 2017, in accordance with these requirements. The unaudited Statement of Accounts

2016/17 was made available on the Council's website from 19 June 2017 in compliance with the Accounts and Audit Regulations 2015.

3. A number of changes have been made to the unaudited Statement of Accounts 2016/17. These changes are mainly to the narrative content, general presentation for the benefit of readers and to the internal consistency and correctness of the figures in notes to the accounts.
4. Also, as a result of the audit there was a revision to the revaluation of the Council's housing stock. The result of this was to reduce their assessed valuation at 31 March 2017 from £263.2m to £255.6m a reduction of £7.6m. A summary of the balance sheet changes is set out in the table below.

Balance Sheet Changes 2016/17

| | Unaudited £000 | Audited £000 | Change £000 |
|-----------------------------|-----------------------|-----------------------|----------------------|
| Property, Plant & Equipment | 320,059 | 312,401 | -7,658 |
| Other assets & liabilities | -124,389 | -124,389 | - |
| Net Assets | <u>195,670</u> | <u>188,012</u> | <u>-7,658</u> |
| Usable Reserves | 28,664 | 28,664 | - |
| Unusable Reserves | 167,006 | 159,348 | -7,658 |
| Total Reserves | <u>195,670</u> | <u>188,012</u> | <u>-7,658</u> |

5. Through the Committee resolving to approve the audited Statement of Accounts, the Section 151 Officer together with the Chairman of the Committee will need to sign a letter of representation on behalf of the Committee and Council to KPMG, to enable the audit opinion to be issued. The signing of this letter is consistent with established protocols, the requirements of KPMG and the general delegations to the S151 Officer. This letter is a formal written record of the representations being made on behalf of the Council via the committee; it deals with the processes and procedures the Council adopts to ensure that it is in compliance with statutory requirements, laws and regulations and also confirms there is a sufficiently robust management system to prevent and detect fraud and irregularities.
6. In addition, Regulation 9 requires that the Statement of Accounts should be signed and dated by the Chair presiding at the Audit and Standards Committee meeting at which approval is given. That regulation also requires the Statement of Accounts to be published with the Independent auditor's report to the members of Stroud District Council. This report is in the Statement of Accounts Appendix A.
7. The Council's external auditors KPMG also present separately to this meeting their 'Report to those charged with governance (ISA 260) 2016/17',

which summarises their finding arising from their audit of the Statement of Accounts.

8. The Statement of Accounts is comprised of four main statements as required by International Financial Reporting Standards which are:-

- **Movement in Reserves Statement**

This is split between usable and unusable reserves and shows the detail of movement in reserves, from the surplus / (deficit) on provision of services in the Comprehensive Income and Expenditure Statement (CIES), to the position on the Balance Sheet at 31 March 2017.

- **Comprehensive Income and Expenditure Statement**

The CIES consolidates all the financial gains and losses experienced during the year. The CIES has two sections:

- a) Surplus or Deficit on the Provision of Services – which shows the increase or decrease in the net worth of the Council as a result of incurring expenses and generating income.
- b) Other Comprehensive Income and Expenditure – which shows any other changes to net worth, and examples include movements in the fair value of assets or actuarial gains or losses on pension assets and liabilities.

- **Balance Sheet**

The Balance Sheet summarises the Council's financial position at 31 March 2017. The top half shows accrued assets and liabilities. The bottom half is comprised of reserves, split between usable and unusable reserves, which represent the net worth of the Council.

- **Cash Flow Statement**

This shows the year on year change in cash and cash equivalents, which are cash on call, and investments with a maturity of three months or less.

A new Note called **Expenditure and Funding Analysis** is included prominently on page 14 of the Statement of Accounts. This links the figures in the Comprehensive Income and Expenditure Statement to outturn figures reported to each of the Council's committees.

9. A full revised version of the accounts is enclosed at Appendix A, and has also been deposited in the Members' Lounge for inspection. Once the accounts are approved a copy will be made available on the Council's internet site together with the Annual Governance Report <http://www.stroud.gov.uk/council/public-notice/public-audit-of-accounts-for-the-year-ended-31-March-2017>.

STROUD DISTRICT COUNCIL
AUDIT AND STANDARDS COMMITTEE

**AGENDA
ITEM NO**

12 SEPTEMBER 2017

8

| Report Title | INTERNAL AUDIT ACTIVITY PROGRESS REPORT 2017/18 |
|---|--|
| Purpose of Report | To inform Members of the Internal Audit activity progress in relation to the approved Internal Audit Plan 2017/18. |
| Decisions(s) | <p>The Committee RESOLVES to:</p> <ul style="list-style-type: none"> • Accept the progress against the Internal Audit Plan 2017/18; • Accept the assurance opinions provided in relation to the effectiveness of the Council's control environment comprising risk management, control and governance arrangements as a result of the Internal Audit activity completed to date; and • Request senior management attendance at the next meeting of the Committee to provide an update on the actions taken in relation to the recommendations made in the Local Government Pension Scheme (LGPS) 2014 internal audit report, which contained a split assurance opinion of Limited/Satisfactory for control environment. |
| Consultation and Feedback | Internal Audit findings are discussed with Service Heads/Managers. Management responses to recommendations are included in each assignment report. |
| Financial Implications and Risk Assessment | <p>There are no financial implications arising from the report.</p> <p>Graham Bailey Principal Accountant Tel: 01453 754133 Email: graham.bailey@stroud.gov.uk</p> <p>Risk Assessment:</p> <p>Failure to deliver an effective Internal Audit service will prevent an independent, objective assurance opinion from being provided to those charged with governance that the key risks associated with the achievement of the Council's objectives are being adequately controlled.</p> |

| | |
|---|--|
| Legal Implications | There are no legal implications to highlight. (Ref: r22.8c24.8d29.8) Karen Trickey, Legal Services Manager and Monitoring Officer Tel: 01453 754369 Email: karen.trickey@stroud.gov.uk |
| Report Author | Theresa Mortimer Head of Audit Risk Assurance (Chief Internal Auditor) Tel: 01453 754111 Email: theresa.mortimer@stroud.gov.uk |
| Options | There are no alternative options that are relevant to this matter. |
| Performance Management Follow Up | In accordance with the Public Sector Internal Audit Standards 2017 (PSIAS) and reflected within the Audit and Standards Committee work programme, Internal Audit reports on progress against the approved Internal Audit Plan 2017/18. These are scheduled to be presented to the Audit and Standards Committee at the November 2017, February 2018 and April 2018 meetings. |
| Background Papers/ Appendices | Appendix A – Internal Audit Activity Progress Report 2017/18. Background papers: <ul style="list-style-type: none"> ➤ Internal Audit Plan 2017/18; ➤ PSIAS; and the ➤ CIPFA Local Government Application Note for the UK PSIAS. |

1.0 Background

1.1 Members approved the Internal Audit Plan 2017/18 at 11th April 2017 Audit and Standards Committee meeting. In accordance with the Public Sector Internal Audit Standards 2017 (PSIAS), this report (through **Appendix A**) details the outcomes of Internal Audit work carried out in accordance with the approved Plan.

1.2 The Internal Audit Activity Progress Report 2017/18 at **Appendix A** summarises:

- The progress against the 2017/18 Internal Audit Plan, including the assurance opinions on the effectiveness of risk management and control processes;
- The outcomes of the Internal Audit activity during the period June 2017 to September 2017;
- Special investigations/counter fraud activity; and
- The Housing Revenue Account (HRA) balances internal audit further review report.

- 1.3 The report is the first progress report in relation to the Internal Audit Plan 2017/18. It is noted that the outcomes of the Banks Automated Clearing System (BACS) internal audit 2017/18 were reported to the July 2017 Audit and Standards Committee.

Internal Audit Activity Progress Report

2017-2018



Audit and Standards Committee
12 September 2017



Appendix A
Agenda Item 8

(1) Introduction

All local authorities must make proper provision for internal audit in line with the 1972 Local Government Act (S151) and the Accounts and Audit Regulations 2015. The latter states that a relevant authority “must undertake an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes, taking into account public sector internal auditing standards or guidance”. The Internal Audit Service is provided by Audit Risk Assurance under a Shared Service agreement between Stroud District Council, Gloucester City Council and Gloucestershire County Council and carries out the work required to satisfy this legislative requirement and reports its findings and conclusions to management and to this Committee.

The guidance accompanying the Regulations recognises the Public Sector Internal Audit Standards 2017 (PSIAS) as representing “proper internal audit practices”. The standards define the way in which the Internal Audit Service should be established and undertake its functions.

(2) Responsibilities

Management are responsible for establishing and maintaining appropriate risk management processes, control systems (financial and non financial) and governance arrangements.

Internal Audit plays a key role in providing independent assurance and advising the organisation that these arrangements are in place and operating effectively.

Internal Audit is not the only source of assurance for the Council. There are a range of external audit and inspection agencies as well as management processes which also provide assurance and these are set out in the Council’s Code of Corporate Governance and its Annual Governance Statement.

(3) Purpose of this Report

One of the key requirements of the standards is that the Chief Internal Auditor should provide progress reports on internal audit activity to those charged with governance. This report summarises:

- The progress against the 2017/18 Internal Audit Programme, including the assurance opinions on the effectiveness of risk management and control processes;
- The outcomes of the Internal Audit activity during the period June 2017 to September 2017;
- Special investigations/counter fraud activity; and

- The outcomes of the Housing Revenue Account (HRA) Balances final follow up review.

(4) Progress against the 2017/18 Internal Audit Programme, including the assurance opinions on risk and control

The schedule provided at **Attachment 1** provides the summary of 2017/18 audits which have not previously been reported to the Audit and Standards Committee.

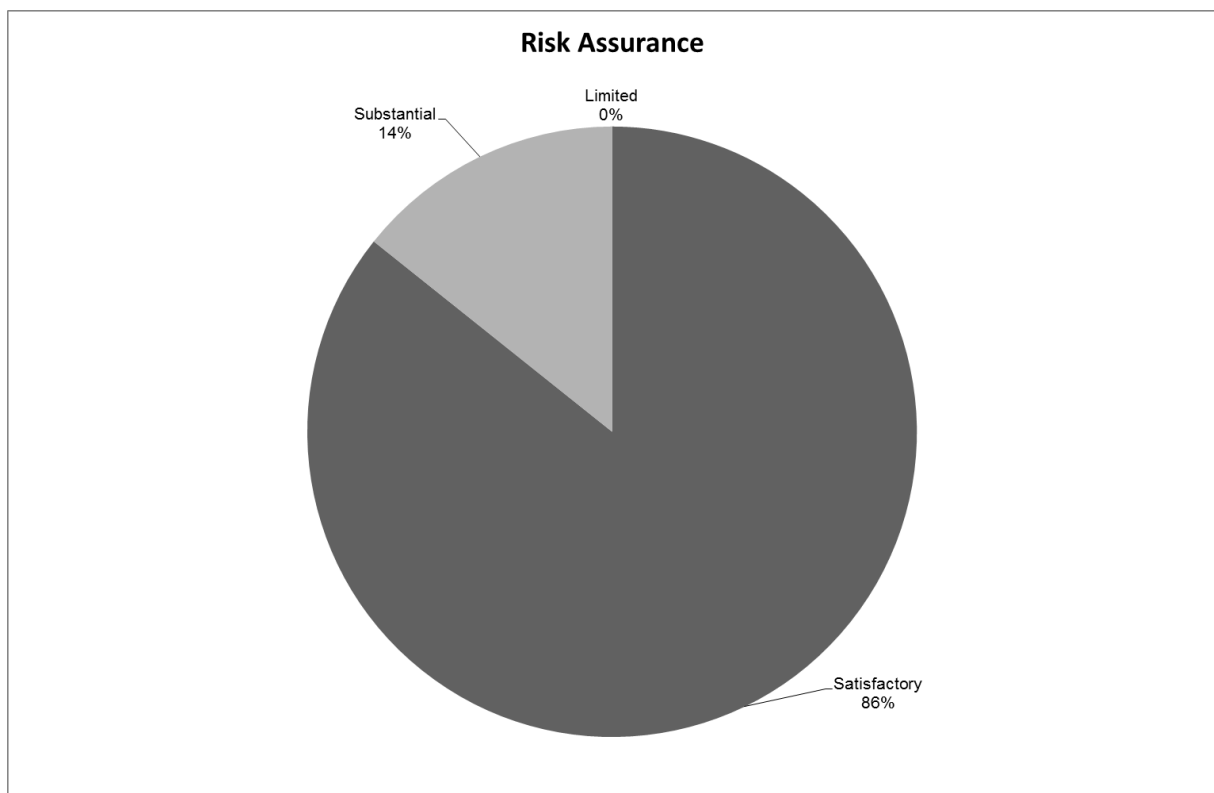
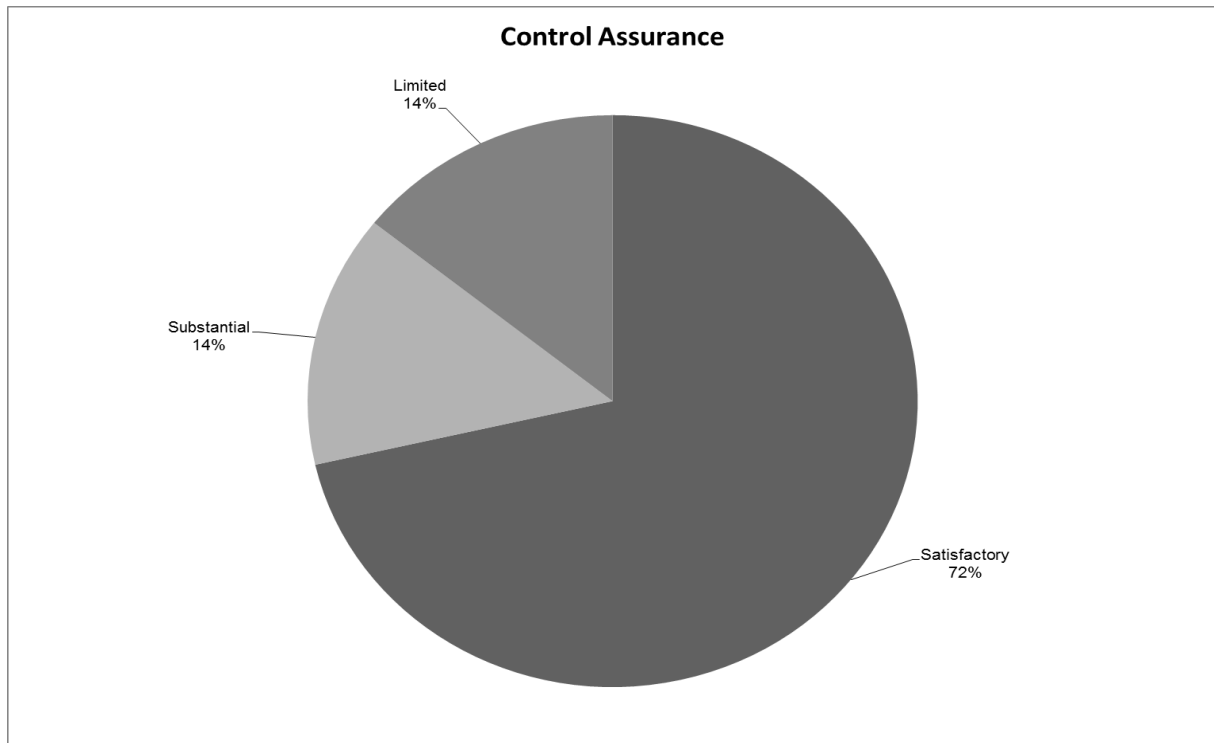
Attachment 2 includes the HRA Balances final follow up review summary.

The schedule provided at **Attachment 3** contains a list of all of the 2017/18 Internal Audit Plan activity undertaken during the financial year to date, which includes, where relevant, the assurance opinions on the effectiveness of risk management arrangements and control processes in place to manage those risks and the dates where a summary of the activities outcomes has been presented to the Audit and Standards Committee. Explanations of the meaning of these opinions are shown in the below table.

| Assurance Levels | Risk Identification Maturity | Control Environment |
|---------------------|---|---|
| Substantial | Risk Managed Service area fully aware of the risks relating to the area under review and the impact that these may have on service delivery, other service areas, finance, reputation, legal, the environment, client/customer/partners, and staff. All key risks are accurately reported and monitored in line with the Council's Risk Management Policy. | <ul style="list-style-type: none"> • System Adequacy – Robust framework of controls ensures that there is a high likelihood of objectives being achieved • Control Application – Controls are applied continuously or with minor lapses |
| Satisfactory | Risk Aware Service area has an awareness of the risks relating to the area under review and the impact that these may have on service delivery, other service areas, finance, reputation, legal, the environment, client/customer/partners, and staff, however some key risks are not being accurately reported and monitored in line with the Council's Risk Management Policy. | <ul style="list-style-type: none"> • System Adequacy – Sufficient framework of key controls for objectives to be achieved but, control framework could be stronger • Control Application – Controls are applied but with some lapses |
| Limited | Risk Naïve Due to an absence of accurate and regular reporting and monitoring of the key risks in line with the Council's Risk Management Policy, the service area has not demonstrated a satisfactory awareness of the risks relating to the area under review and the impact that these may have on service delivery, other service areas, finance, reputation, legal, the environment, client/customer/partners and staff. | <ul style="list-style-type: none"> • System Adequacy – Risk of objectives not being achieved due to the absence of key internal controls • Control Application – Significant breakdown in the application of control |

(4a) Summary of Internal Audit Assurance Opinions on Risk and Control

The pie charts below show the summary of the risk and control assurance opinions provided within each category of opinion i.e. substantial, satisfactory and limited in relation to the audit activity undertaken during the period April 2017 to September 2017.



(4b) Limited Control Assurance Opinions

Where audit activities record that a limited assurance opinion on control has been provided, the Audit and Standards Committee may request Senior Management attendance to the next meeting of the Committee to provide an update as to their actions taken to address the risks and associated recommendations identified by Internal Audit.

(4c) Audit Activity where a Limited Assurance Opinion has been provided on Control

During the period June 2017 to September 2017, one audit review has been provided with a split assurance opinion of Limited/Satisfactory for control environment. This relates to the Local Government Pensions Scheme (LGPS) 2014 internal audit report, where limited assurance was applied to four key control areas only (see **Attachment 1**).

Within 2016/17, one limited opinion on control was provided in relation to ICT Business Processes. The audit outcomes were presented to the July 2017 Audit and Standards Committee. Management update on actions taken following the ICT Business Processes internal audit are to be presented at a scheduled Members meeting. Audit follow up of the management actions will then be completed later within 2017/18 and the outcomes presented to Audit and Standards Committee.

(4d) Satisfactory Control Assurance Opinions

Where audit activities record that a satisfactory assurance opinion on control has been provided, where recommendations have been made to reflect some improvements in control, the Committee can take assurance that improvement actions have been agreed with management to address these.

(4e) Internal Audit Recommendations

During the period June 2017 to September 2017 Internal Audit made, in total, **24** recommendations to improve the control environment, **6** of these being high priority recommendations (**100%** of these being accepted by management) and **18** being medium priority recommendations (**100%** accepted by management).

The Committee can take assurance that all high priority recommendations will remain under review by Internal Audit, by obtaining regular management updates, until the required action has been fully completed.

(4f) Risk Assurance Opinions

During the period June 2017 to September 2017, it is pleasing to report that no limited assurance opinions on risk have been provided on completed audits from the 2017/18 Internal Audit Plan.

Where a limited assurance opinion is given, the Shared Service Senior Risk Management Advisor will be provided with the Internal Audit report(s) to enable the prioritisation of risk management support.

Completed Internal Audit Activity during the period June 2017 to September 2017

Summary of Limited Assurance Opinions on Control

Service Area: Finance

Audit Activity: Local Government Pension Scheme Regulations 2014

Background

In April 2014 the Local Government Pension Scheme (LGPS) was revised. The new scheme known as LGPS14 is a career average pension scheme rather than a final salary scheme.

Existing employees' future pensions are protected in respect of their pre-2014 service. Their pensions are now made up of a final salary element for the pre-2014 service and a career average re-valued earnings (CARE) element for the post 2014 service.

As a result, employers are required to keep additional information on members' salaries and contributions and to provide the Gloucestershire Pensions Administration Section with an annual return by 31st May each year (CARE report).

It is essential that the information provided to the Pensions Administration Section is correct and accurate, as the new LGPS regulations now require that each member's actual benefits for the year are calculated, allocated and notified to the member by 31st August following the end of each financial year.

Stroud District Council (SDC) took over the administration of the payroll function on 1st April 2016; for the seven years prior to this it was run by an external provider. As at 31st March 2016 there were 468 SDC employees who were active members of the LGPS scheme.

Scope

- Compliance with the Payroll Guide to the 2014 Scheme including;
 - Treatment of non-contractual overtime;
 - Assumed pensionable pay for those on child related leave and sick leave;
 - Breaks in membership of the scheme and membership of the 50:50 scheme;
 - Additional pension contributions;
 - Salary sacrifice schemes; and
 - Employer and employee contributions.

- To review year-end CARE report, processes, controls and accuracy; and
- To review the completion of leavers forms.

Risk Assurance - Satisfactory**Control Assurance - SPLIT OPINION - Satisfactory/Limited****Key Findings**

Overall it was found that the administration of the pension scheme is satisfactory with deductions being correctly made for both employees and employers in the majority of cases. Monthly and annual returns are submitted promptly.

There are 33 cases, in the 2015/16 return submitted in May 2016, where the number of records on the annual return for an individual at the year end did not match the number of records held in the pension scheme database. This could be due to errors by SDC or Gloucestershire Pension Fund (Pensions). There should be a separate line of information for each separate contract that an employee has. Pensions have not brought these anomalies to the attention of SDC and therefore they remain unresolved. As a result, individuals concerned have not received annual benefit statements.

Internal Audit found that certain areas specifically referred to in the LGA guidance were not operating as intended. In particular:

- Assumed pensionable pay for individuals on sickness and maternity leave was found not to be correct. This should be based on the average pensionable pay for the three months prior to the start of the leave. The same amount is then applied each month. In the cases reviewed the amount altered from month to month and it was not clear how it was calculated. Management have put in a request to the payroll software provider to investigate the matter.
- A scheme is in place to enable staff to purchase additional annual leave. The treatment of this scheme from a taxation/pensions perspective does not appear to be correct. Further advice from our tax advisers and liaison by the advisers with HMRC and the pension fund will lead to a resolution of this issue.
- When an individual leaves the organisation if they were a member of the LGPS prior to 1st April 2014 part of their pension will be based on their final salary. The final salary is calculated as it would have been under the 2008 regulations, when for example non-contractual payments such as overtime were not pensionable. Finance is required to provide the pensionable pay under the 2008 regulations for this purpose. Finance did not appreciate that

the pensionable pay required was not the current pensionable pay. That said they have broken down any payments over and above the basic salary and as a result Pensions have been able to raise questions and the correct pension calculated.

- Internal Audit found that in three out of six records tested Pensions had not been informed of contractual changes in advance of the individual leaving. As well as ensuring that in future Pensions are informed, management should consider undertaking some checking of service history records held by Pensions.

Conclusion

Under the LGPS scheme the employer has responsibilities for fully understanding and implementing the guidance. Therefore it is important that SDC fully understand the regulations and provide accurate information to the Gloucestershire Pensions Administration Section.

Although overall SDC administration of the scheme is satisfactory, where Internal Audit has identified errors, these demonstrate that either Finance does not understand the legislation and/or that they have not tested the payroll system to ensure that it is correctly configured. The errors identified only affect a limited number of employees.

Management Actions

Management have responded positively to the nine audit recommendations that have been made, of which five are classified as high priority and relate to the Key Findings four bullet points.

Summary of Satisfactory Assurance Opinions on Control

Service Area: Council Wide

Audit Activity: Network Access Controls

Background

As part of the 2016/17 internal audit plan approved by the Stroud District Council (SDC) Audit and Standards Committee, a review of Network Access Controls was undertaken.

Scope

The scope of this audit encompassed both Access Controls and the ICT Control Environment.

Access Controls:

- Validity of Active Directory access rights;
- Authorisation and user set up;
- Leaver access rights are promptly disabled; and
- Review of privilege user access rights.

ICT Control Environment:

- Documented and comprehensive ICT security policy framework;
- Active Directory password and account lockout security settings; and
- External penetration testing.

Risk Assurance – Satisfactory

Control Assurance – Satisfactory

Key Findings

Audit testing confirmed that the SDC network domain was subject to annual external penetration testing in December 2016. All reported network vulnerabilities from the most recent penetration test have been addressed by the Council. Public Services Network (PSN) Code of Connection was attained by the Council on 27 February 2017.

Comprehensive information security policy guidelines have been published on the SDC intranet which includes guidance on the risk of cyber security threats such as ransomware. All Active Directory new user access requests are submitted via the SDC intranet and authorised by the respective line manager. Robust password policies and account lockout policies have been invoked on the Active Directory domain. The SDC Human Resources team extract monthly reports of all leavers from the Agresso payroll system. Details are then passed to ICT who promptly disabled leaver access rights.

Conclusions

The internal audit has resulted in satisfactory assurance levels for both risk identification maturity and control environment. Some development actions have been identified, to support improvement of internal controls. The main areas that require attention are:

- The need to assess the feasibility of disabling the default administrator account;
- A review to assess the validity and necessity of all service accounts that have been allocated superuser access rights; and
- The failure to enable audit policies on the Active Directory domain.

Management Actions

Management have responded positively to the Internal Audit recommendations made.

Service Area: Finance

Audit Activity: Council Tax Opening Debit – 2017/18

Background

Council Tax is a system of local taxation collected by local authorities and is a tax on domestic property collected by Stroud District Council. All homes are given a Council Tax valuation band (A to H) by the Valuation Office Agency (VOA), which is based on the value of the property on 1st April 1991. Newly constructed properties are also assigned a nominal 1991 value by the VOA.

The Council meeting on 23rd February 2017 recorded the Council Tax requirement for the Council's own purposes and other 'precepting' authorities to be:

| | |
|--------------------------------|-------------|
| Stroud District Council | £8,354,121 |
| Gloucestershire County Council | £50,353,514 |
| Police and Crime Commissioner | £9,158,577 |
| Parish and Town Councils | £3,330,955 |

Scope

An audit of the Council Tax opening debit was undertaken to provide assurance that the Council Tax opening debit has been correctly calculated and reflected in the Council Tax system.

Risk Assurance – Satisfactory

Control Assurance – Satisfactory

Key Findings

Revenue and Benefits acknowledge the inherent associated risks and mitigating controls relating to the Council Tax opening debit and have captured these using the corporate system for risk recording (Excelsis).

Finance collated the Council Tax budget requirements and using the tax base information, determined the Band 'D' charges for all residents in the Parish/Town areas. This was reviewed and authorised by the Accountancy Manager as part of his delegated powers as acting Section 151 Officer.

A reconciliation of the total number of properties by band between the VOA (as at 12th February 2017) and the CIVICA Open Revenues System (CIVICA) was conducted and signed by the Revenue Officer.

Revenue and Benefits updated CIVICA with the Finance calculated band 'D' rates. These were verified and signed by a team member and the Revenue and Benefits Manager.

Before updating the CIVICA system with the new household Council Tax rates, Revenue and Benefits tested the process in the CIVICA Test System. Once it was confirmed that the updates on the CIVICA Test System were accurate, the CIVICA Live System was updated.

The Revenue and Benefits team received letter samples to check the formatting and accuracy of the billing. In addition, the Revenue and Benefits Manager checked the Council Tax total value with the total value of the letters and once this matched the letters were approved for posting.

Conclusions

The audit confirmed that there is a sound Council Tax Opening Debit control framework in place to:

- Receive the precepts from Gloucestershire County Council, Gloucestershire Police Authority and the Parish/Town Councils;

- Calculate the Band 'D' charges for all residents;
- Return the 'Council Tax Requirement Return' to the Department for Communities and Local Government;
- Reconcile properties held by the VOA with CIVICA;
- Check and update CIVICA with the new rates; and
- Check and print the Council Tax letters.

Internal Audit has made one medium priority recommendation with the aim to further strengthen the control environment in respect of documenting reconciliation activities.

Management Actions

Management have responded positively to the one medium recommendation made.

Service Area: Tenant and Corporate Services

Audit Activity: Brimscombe Port Redevelopment

Background

Brimscombe Port is a ten acre brownfield site in an industrial heritage conservation area and although currently infilled it is seen as a key part of the Cotswold Canals with significant historical and cultural value.

Brimscombe Port was transferred to the Stroud Valleys Canal Company (SVCC) from British Waterways in 2009, utilising grant funding of £7.6m from the South West Regional Development Agency. In 2015 the Housing and Communities Agency (HCA) approached Stroud District Council to discuss additional funding to bridge the funding gap and bring the site forward for redevelopment with the expectation of delivering the outcome of the South West Regional Development Agency's original investment in the site. The HCA agreed to invest a further £2m, by way of a recoverable loan, with Stroud District Council contributing £1m of capital monies to fund site preparation.

The HCA's investment is repayable and will be triggered upon the development and sale of the site. Both the HCA's and Stroud District Council's funding are conditional upon the site transferring from SVCC to the Council, as the accountable body and the organisation that will deliver the redevelopment of the site. However, once the works are completed, the remediated canal and port basin of Brimscombe Port will be transferred back to SVCC.

Scope

An audit was undertaken to provide assurance that the project management of the site preparation of the Brimscombe Port redevelopment meets the requirements of the Council's project management guidance and expectations.

Risk Assurance – Satisfactory**Control Assurance – Satisfactory****Key Findings**

As part of the review Internal Audit met with two Councillors, the Project Board, and the Project Team; reviewed Committee and team documentation; and accessed the South West Procurement Portal. Findings included:

- The governance for the project is provided by a Project Sponsor, the Strategy and Resources Committee, the Investment and Development Panel, the Brimscombe Port Project Board and the Brimscombe Port Project Team.
- Project Board meetings are held every six weeks and evidence open and transparent discussions with good challenging of the Project Team, and particular focus on project milestones and financial governance.
- The Project Board Terms of Reference could be improved with the addition of a clearly defined decision making framework.
- In addition to the core membership of the Project Board, key professionals are invited to help inform decision making. To ensure compliance with Stroud District Council's Financial Regulations the Section 151 Officer can nominate a member of staff from Financial Services who will give advice as needed. The Project Manager is aware of this requirement and going forward will seek advice as appropriate.
- The New Homes and Regeneration Manager uses an expenditure spreadsheet to manage and monitor the project finances, which is presented to the Project Board as a standing agenda item for review.
- In May 2017, the Project Team structure was reviewed resulting in a new Project Manager and two new team members. Internal Audit has observed that the new team structure is having a positive impact upon the project, with significant improvements in project documentation; and the Project Manager and the team demonstrating a good understanding of the project, milestones, risks and project outputs.

- The project plan documents 98 tasks. Although up-to-date and regularly monitored its effectiveness could be improved through reviews of project tasks, baselines, milestones and resources. This will ensure increased transparency of the project position and that the Project Team and Project Board are supported in their decision making.
- As at the time of the audit, an Options Appraisal was being developed and Internal Audit was assured by the Project Manager that it would be complete and presented to the Project Board by October 2017.
- Asset Management has acknowledged an associated inherent risk relating to the Brimscombe Port redevelopment and has captured this using the corporate system for recording, Excelsis.
- In June 2017, the Project Team reviewed and updated all risks in the Brimscombe Port Risk Register spreadsheet, resulting in 30 identified risks, four of which have been classified with a very high inherent risk score. These are regularly reviewed and presented to the Project Board as a standing agenda item.
- The Project Team are aware of the Council's Procurement process and followed it when the Civil Engineer contract was awarded. This was verified by Internal Audit when reviewing the South West Procurement Portal.
- The Project Team have considered various legislative and corporate requirements such as the Public Services (Social Value) Act, the Localism Act (2011) and the Corporate Consultation Strategy.

Conclusions

As at the date of the review, Internal Audit are able to confirm that there is evidence of sound project management of the site preparation of the Brimscombe Port redevelopment which meets the requirements of the Council's project management guidance and expectations.

Internal Audit has worked closely with the service area providing professional advice and support as required to aid project management and has made three recommendations to further strengthen arrangements over project governance and project management (including risk management).

Management Actions

Management have responded positively to the three medium recommendations made.

Service Area: Tenant and Corporate Services**Audit Activity: Response Repairs Contract****Background**

Tenant Services have had a number of contracts in place to deliver asset management services to its housing stock of 5,117 Council rented dwellings.

In October 2015 Stroud District Council went through a procurement process for works to be let as two contracts to two separate contractors; with an annual value anticipated to be £4 million per contract. The contracts are for four years with the option to extend for a further six years by two separate extensions of up to three years each. From 17:00 31st March 2016, two contracts were let for the north and south of the district; the contract for the north was awarded to NKS Contracts (Central) Ltd and south to Mears Ltd.

The contracts are aimed at dealing with responsive repairs i.e. day to day minor repairs that need to be dealt with quickly to keep properties in reasonable order and to a lettable standard, work to void properties to enable properties to be re-let, and planned elemental upgrade works such as replacement of kitchens, bathrooms and roofs.

Scope

The review sought to provide assurance that:

- There are effective arrangements in place to manage and monitor the contractors Key Performance Indicators (KPI's);
- There is a robust decision making process for work order variations that ensure the prevention of unnecessary works; and
- There is a sound control framework to monitor contractual compliance for safeguarding vulnerable residents.

During the audit, the scope of the review was increased to include the accuracy of raised work orders and the use of the 'Minimum Order' rate, due to the findings emanating from the monthly audit reports that are produced by an external consultant.

Risk Assurance – Satisfactory**Control Assurance – Satisfactory**

Key Findings

Risk Management

Tenant Services have acknowledged the inherent associated risks and mitigating controls generically for Tenant Services contracts and have captured these under three references using the corporate system for risk recording (Excelsis). Internal Audit has recommended that an additional risk for managing the safeguarding of vulnerable tenants is included within Excelsis. In addition, focus now needs to be given to ensure that identified risks are periodically reviewed and updated in line with the target review dates set on Excelsis.

KPI's

The Maintenance and Void Works element of the contract has ten KPI's and the Planned Works element of the contract has six KPI's. A representative sample of KPI's was selected by Internal Audit and it was found that:

- Some KPI's are calculated by Tenant Services and others by the contractors;
- Tenant Services do not independently verify contractor calculated KPI's;
- Planned Work KPI's are only calculated for one of the two contractors; and
- KPI calculations are not consistently accurate.

Tenant Services management have agreed to review and refresh the suite of KPI's to ensure that KPI's are fit for purpose and enable more robust management of the contractors' performance. Going forward all KPI's will be generated by Tenant Services to ensure consistency and accuracy.

Work Orders and Variations

Internal Audit found that there is a clear process for raising and authorising work orders. When a work order is raised, Tenant Services assign codes for each element of the work e.g. codes for each part required and type of labour needed.

As part of contract management, Tenant Services have engaged an external consultant to review work orders and their codes for accuracy. Sampling of work orders, for the period July 2016 to March 2017 found that an average of 57% of sampled work orders potentially had incorrect codes; however Tenant Services' decision to use these codes may have clear justification and give due consideration to best value when remedying the work required.

Tenant Services having considered the consultants findings, have concluded that actions will be taken to rectify the identified issues. Further work is now needed by Tenant Services to quantify the financial value of the incorrect code usage and management are proactively seeking to ensure the current review process is enhanced and key learning points are shared with applicable staff.

The contract allows for a minimum value to be paid for work orders, this is variable depending upon the type of work required. The majority of these are applied to low value work orders to ensure a minimum payment of £25. From a sample of 25 work orders, between April 2016 and May 2017 where a minimum order code was applied, Internal Audit found that 52% had an incorrect minimum order value resulting in a £207.09 overpayment to the contractors. Subsequent to the audit, Tenant Services are proactively reviewing work orders to ensure that they are accurate and any identified payments are addressed. Internal Audit have recommended further enhancements to the control environment to ensure the authorisation of work orders are reviewed in line with Tenant Services risk appetite.

There are agreed processes in place that a contractor can follow to request a variation to a Maintenance and Void Works and Planned Works work order.

Tenant Services staff use their experience and work knowledge to check that all work is necessary, however there is no documentary evidence in place to support the checking and rejection of unnecessary work and therefore Internal Audit can give no assurance that in all cases these checks have taken place. However since the audit, a process to record unnecessary work requests is being implemented by Tenant Services.

Safeguarding

Safeguarding training was delivered by Stroud District Council's Sport and Health Development Manager to the contractors, who are responsible for embedding safeguarding training into their company's induction process.

There are systems and processes in place to record when a tenant identifies themselves as vulnerable, however this needs to be enhanced to ensure that staff are confident in identifying and supporting vulnerable tenants.

If a tenant informs Tenant Services that they are vulnerable it is recorded on the Northgate Housing Management System and this information is passed onto the contractor during daytime working hours only and not during 'out of hours'. Tenant Services intend to address this as part of the procurement for the new out of office provider process, in 2017.

The monitoring of contractor's staff DBS (Disclosure and Barring Service) checks needs to be strengthened to ensure that contractors promptly notify Tenant Services that checks have taken place.

Conclusions

Internal Audit is pleased to confirm that there are systems and processes in place for:

- The capturing of risks associated with Tenant Services contracts;
- Acquiring and recording KPI information;
- Contractors to request work order variations;
- The monitoring of work variations that exceed authorisation limits; and
- Contractors to be notified of tenant vulnerability during daytime working hours.

Internal Audit has made five recommendations aimed at strengthening:

- Risk management, and contract management and monitoring;
- KPI's;
- The use and accuracy of the application of the schedule of rates codes;
- The monitoring of work orders; and
- The safeguarding of vulnerable residents.

Management Actions

Management have responded positively to the four medium and one high priority recommendations made.

Summary of Substantial Assurance Opinions on Control

Service Area: Finance

Audit Activity: Benefits Up-rating 2017/18

Background

Stroud District Council's expenditure on Housing Benefits and Council Tax Support was approximately £30m for 2016/17. The rules surrounding entitlement to Housing Benefit and Council Tax Support are very complex and any administrative errors have the potential to lead to under / overpayments.

The Minister of State for Welfare Reform announced, in his written statement to Parliament on 28th November 2016, his proposals for the social security benefit rates that would apply from April 2017. Details of the rates were published in a Housing Benefit Circular available to all Councils to enable them to take the appropriate action.

The Council is responsible for the management and application of the Council Tax Support Scheme that operates in the district. Members at 13th October 2016 Strategy and Resources Committee approved the Council's 2017/18 Local Council Tax Support Scheme.

The Council maintains records of all Housing Benefit and Council Tax Support claims and claimant information on the Benefits system – Civica Open Revenues system.

Scope

This audit was undertaken to provide assurance that Housing Benefit and Council Tax Support rates for 2017/18 had been correctly updated to the Benefits system and that internal procedures had been followed for verifying the rates before they were applied.

Risk Assurance – Substantial

Control Assurance – Substantial

Key Findings

Nationally set increases for 2017/18 Housing Benefits and Council Tax Reduction Scheme parameters were updated to the Benefits system by one officer and independently checked for correct update by a different officer. In addition a random sample of 20 rates and thresholds selected by Internal Audit were agreed to source documentation and the Benefits system.

The Revenue and Benefits Manager provided verbal rather than formal approval to ICT to apply the 2017/18 rates and threshold to the Benefits system.

Sample checks of Benefit claims were performed by Benefit Officers following successful update of the parameters to the Benefits system to confirm the system was correctly applying the 2017/18 rates and thresholds, but documentary evidence of the checks was not retained.

Conclusions

The results of the Internal Audit review confirmed through testing and discussions with appropriate officers that suitable controls were applied to ensure that Housing Benefit and Council Tax Support rates for 2017/18 had been correctly updated to the Benefits system.

Management Actions

Internal Audit has raised three medium priority recommendations to make the process for future years more efficient and for documentary evidence to be retained to support completion of all the controls and key activities involved in the Benefits parameter up-rating process.

Summary of Special Investigations/Counter Fraud Activities

Current Status

During 2017/18 to date (1st April 2017 to 31st July 2017) there have been four potential irregularities referred to Internal Audit relating to tenancy issues.

One of these has been passed to the Department for Work and Pensions (DWP) as the queries raised by a member of the public did not relate to matters dealt with by the Council.

Another case has been closed following a joint investigation with Internal Audit and Tenant Services, concerning an application for social housing. There was insufficient evidence to take the matter further.

Internal Audit is currently working with relevant officers within the Council on the remaining two cases, which involve allegations of subletting.

In addition, Internal Audit continued to provide advice on a subletting / right to buy issue from 2016/17, although did not actively investigate this case. Service decision was made for the case to close within July 2017, due to insufficient evidence to take the matter further.

Any fraud alerts received by Internal Audit from the National Anti-Fraud Network (NAFN) are passed onto the relevant service area within the Council, to alert staff to the potential fraud.

Fraud Risk Assessment/Risk Register

A fraud risk register is currently being developed. The outcome of which will inform future internal audit activity.

National Fraud Initiative (NFI)

Internal Audit continues to support the NFI which is a biennial data matching exercise administered by the Cabinet Office. The data collections were collected throughout October 2016 and reports have been provided for investigation. Examples of data sets include housing, insurance, payroll, creditors, council tax, electoral register and licences for market trader/operator, taxi drivers and personal licences to supply alcohol. Not all matches are investigated but where possible all recommended matches are reviewed by either Internal Audit or the appropriate service area.

In addition, there is an annual data matching exercise undertaken relating to matching the electoral register data to the single person discount data held within the Council. Once all relevant data has been uploaded onto the NFI portal, a data match report is instantly produced and available for analysis.

The outcomes of the review will be provided to the Audit and Standards Committee.

Outcomes from the HRA Balances final follow up review

Service Area: Finance

Audit Activity: Housing Revenue Account (HRA) Final Follow Up

Background

An investigation was undertaken by Internal Audit within 2016/17, following the discovery by Council officers that balances had been overstated within the HRA 2014/15 Outturn report to the Housing Committee. The overstated balance of £909k continued to be included in financial reports throughout 2015/16.

Following the investigation, a report was produced which included eight recommendations; seven high priority and one medium. The investigation outcomes were reported to Audit and Standards Committee in July 2016.

Between September 2016 and March 2017 three follow up reviews were completed and reported to Audit and Standards Committee, to provide an update as to the progress made with the original investigation report recommendations. The March 2017 follow up report (reported to Audit and Standards Committee in April 2017) confirmed that all recommendations had been addressed by management and appropriate actions taken.

A final follow up review is included within the Stroud District Council Internal Audit Plan 2017/18 to consider the Housing Committee Outturn report and Statement of Accounts for the financial year 2016/17, and provide assurance that the original investigation recommendations continue to be followed as agreed.

Scope

The HRA Final Follow Up review considered the original investigation recommendations, including the checking of balances brought and carried forward against the Council's financial accounting system (Agresso) for both the HRA and General Fund, in respect of the financial year 2016/17.

Key Findings

The findings from this follow up review confirm that the Council has actioned all of the eight original investigation recommendations.

Both the HRA Outturn report and the Statement of Accounts were checked for consistency in reporting and against balances held in Agresso. No issues arose once checked against the revised Statement of Accounts.

During another review undertaken within Internal Audit it was noted that, there were inconsistencies within two reports to Members in respect of the Environment Committee meeting held on 6th April 2017 and the Community Services and Licensing Committee meeting on 30th March 2017. Although the headline amounts were correctly recorded and consistent within the reports the narrative below the headings were contradictory in as much as:

- The Community Services and Licensing Committee was informed in the report that the Street Cleansing Service (Environment) is showing a projected underspend whilst it is reported to the Environment Committee that there is a projected overspend in this area.
- Also the Environment Committee is informed that the Grounds Maintenance Service (Community Services and Licensing Committee) is showing a projected underspend when the Community Services and Licensing Committee is told that the Grounds Maintenance Service is projecting an overspend.

Both Committee reports indicate that the narrative was provided by the relevant Service Manager (i.e. the budget holder).

Conclusions

It is pleasing to note that all original investigation recommendations have now been implemented, including the addition to the checklist required in respect of the preparation and publishing of the Statement of Accounts.

Although Key Findings confirm there were contradictory statements within two Committee reports, it is noted that the correct financial information in respect of balances was recorded within the headline of each particular paragraph. Other responsible officers, as well as Finance, need to ensure that their narrative/statements produced for reports to Members are accurate.



Progress Report including Assurance Opinions

| Department | Activity Name | Priority | Activity Status | Risk Opinion | Control Opinion | Reported to Audit and Standards Committee | Comments |
|-----------------------------|---|----------|---------------------|----------------|-----------------|---|--|
| Council Wide | Delivery of Savings Target | High | Audit in Progress | | | | Brought Forward from 2016/17 plan |
| Council Wide | Capital Programme | High | Audit in Progress | | | | |
| Council Wide | Contract Management | High | Planned | | | | |
| Council Wide | Gifts and Hospitality | High | Planned | | | | |
| Council Wide | Information Governance | High | Audit in Progress | | | | |
| Council Wide | Members Allowances and Expenses | Medium | Audit in Progress | | | | |
| Council Wide | Post Project Reviews | High | Planned | | | | |
| Council Wide | Procurement | High | Planned | | | | |
| Council Wide | Banks Automated Clearing System (BACS) | High | Final Report Issued | Satisfactory | Satisfactory | 04/07/2017 | |
| Council Wide | Legacy Software | High | Planned | | | | |
| Council Wide | Data Protection | High | Planned | | | | |
| Council Wide | IT Disaster Recovery follow up | High | Planned | | | | |
| Council Wide | Critical ICT systems back up | High | Audit in Progress | | | | New Activity |
| Council Wide | Network Access Controls | High | Final Report Issued | Satisfactory | Satisfactory | 12/09/2017 | Brought Forward from 2016/17 plan |
| Council Wide | ICT Business Process follow up | High | Planned | | | | |
| Development Services | Community Infrastructure Levy | High | Audit in Progress | | | | |
| Development Services | Licensing (Business Licences) | Medium | Planned | | | | |
| Customer Services | Homelessness | Medium | Planned | | | | |
| Customer Services | Housing - Discretionary Payments | Medium | Planned | | | | |
| Customer Services | Multi Services Contract | High | Draft Report Issued | | | | |
| Customer Services | The Pulse Dursley | Medium | Audit in Progress | | | | |
| Finance | Housing Revenue Account (HRA) Balances final follow up | High | Final Report Issued | Not Applicable | Not Applicable | 12/09/2017 | |
| Finance | Benefits Uprating 2017/18 | High | Final Report Issued | Substantial | Substantial | 12/09/2017 | |
| Finance | Budget Setting | High | Planned | | | | |
| Finance | Cash and Bank | High | Audit in Progress | | | | |
| Finance | Council Tax Opening Debit - 2017/18 | High | Final Report Issued | Satisfactory | Satisfactory | 12/09/2017 | |
| Finance | General Ledger | High | Audit in Progress | | | | |
| Finance | National Non Domestic Rates (NNDR) | High | Audit in Progress | | | | |
| Finance | Local Government Pension Scheme Regulations (LGPS) Regulations 2014 | High | Final Report Issued | Satisfactory | Limited | 12/09/2017 | Brought Forward from 2016/17 plan Split opinion on control Satisfactory/Limited |
| Tenant & Corporate Services | Response Repairs Contract | High | Final Report Issued | Satisfactory | Satisfactory | 12/09/2017 | Brought Forward from 2016/17 plan |
| Tenant & Corporate Services | Brimscombe Port Redevelopment | High | Final Report Issued | Satisfactory | Satisfactory | 12/09/2017 | |

STROUD DISTRICT COUNCIL

AGENDA
ITEM NO

AUDIT AND STANDARDS COMMITTEE

12 SEPTEMBER 2017

9

| | |
|---|--|
| Report Title | 1ST QUARTER TREASURY MANAGEMENT ACTIVITY REPORT 2017/18 |
| Purpose of Report | To provide an update on treasury management activity as at 30/06/2017. |
| Decision(s) | The Audit and Standards Committee APPROVES the treasury management activity first quarter report for 2017/2018. |
| Consultation and Feedback | Capita Asset Services Limited |
| Financial Implications & Risk Assessment | Interest of £45k in the first quarter is on target to achieve £180k for 2017/18. Graham Bailey, Principal Accountant Tel: 01453 754133 E-mail: graham.bailey@stroud.gov.uk |
| Legal Implications | There are no significant legal implications. (Ref :r21.8c22.8d25.8) Karen Trickey, Legal Services Manager Email : karen.trickey@stroud.gov.uk |
| Report Author | Maxine Bell, Snr Accounting Officer Tel: 01453 754134 E-mail: maxine.bell@stroud.gov.uk |
| Options | None |
| Performance Management Follow Up | Further quarterly reports and a full 2017/18 annual report. |
| Appendices | A – Economic Update B – Prudential Indicators as at 30 June 2017 C – Explanation of prudential indicators |

Background

1. Treasury management is defined as: 'The management of the local authority's 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.'
2. This report is presented to the Audit and Standards Committee to provide an overview of the investment activity and performance for the first quarter of the financial year, and to report on prudential indicators and compliance with treasury limits. A quarterly report is regarded as good practice, but is not essential under the Code of Practice for Treasury Management (the Code).

Discussion

3. The Chartered Institute of Public Finance and Accountancy (CIPFA) issued the revised Code in November 2011, originally adopted by this Council on 21 January 2010. This first quarter report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:
 - An economic update – Appendix A
 - A review of the Treasury Management Strategy Statement (TMSS) and Investment Strategy
 - A review of the Council's investment portfolio for 2017/18
 - A review of the Council's borrowing strategy for 2017/18
 - A review of compliance with Treasury and Prudential Limits for 2017/18.
 - Other Treasury Issues

Treasury Management Strategy Statement and Investment Strategy update

4. The TMSS for 2017/18 was approved by Council on 23 February 2017. The Council's Investment Strategy, which is incorporated in the TMSS, outlines the Council's investment priorities as follows:
 1. Security of Capital
 2. Liquidity
 3. Yield
5. The Council will also aim to achieve the optimum return on investments commensurate with the proper levels of security and liquidity. In the current economic climate it is considered appropriate to keep investments short term, less than 1 year, with highly credit rated financial institutions, using Capita's suggested creditworthiness approach, which includes a sovereign credit rating and Credit Default Swap (CDS) overlay. The Council is prepared to invest for up to 366 days with UK Government supported banks. Where possible the Council has invested for 3, 6, 9 or 12 month periods to benefit from higher interest rates, otherwise using call accounts.
6. A breakdown of the Council's investment portfolio as at 30 June 2017 is shown in Table 2 of this report. Investments & borrowing during the year have been in line with the strategy.
7. Capita's latest economic analysis is set out in Appendix A. Current advice from Capita is to invest for no more than a year with UK banks, or up to a maximum of five years with government or local government provided they are sufficiently highly rated on Capita's weekly list.

Investment Portfolio 2017/18

8. In accordance with the Code, it is the Council's priority to ensure security and liquidity of investments, and once satisfied with security and liquidity, to obtain a good level of return. The investment portfolio yield for the first quarter is shown in the table below:

TABLE 1: Average Interest Rate Compared With Benchmark Rates

| Period | Investment Interest Earned | Average Investment | Average Interest Rate | Benchmark 7 day LIBID | Benchmark 3 month LIBID |
|---------------------|-----------------------------------|---------------------------|------------------------------|------------------------------|--------------------------------|
| 01/04/17 - 30/06/17 | £43,103 | £33.207m | 0.52% | 0.11% | 0.17% |

9. The Local Area Mortgage Scheme investment of £1m which matured on the 24th April 2017 at 3.8% with Lloyds is excluded from the above table. If this interest is included the interest earned is £45k at an average interest rate of 0.55%.
10. Table 2 below shows the investments and borrowing position at the end of June 2017.
11. The approved limits as set out in the Treasury Management Strategy report to Council 23rd February 2017 within the Annual Investment Strategy were not breached during the first 3 months of 2017/18.
12. Funds were available for investment on a temporary basis. The level of funds available was mainly dependent on the timing of precept payments, receipt of grants and progress on the Capital Programme and canal project. The authority holds £8m core cash balances for investment purposes (i.e. funds that potentially could be invested for more than one year).

TABLE 2: Investments and Borrowing as at June 2017

| | June 2017 £'000 |
|-----------------------------------|----------------------------|
| Federated Prime Rate | 1,900 |
| Deutsche | 1 |
| Goldman Sachs | 1 |
| Money Market Funds Total | 1,902 |
| Bank of Scotland | 3,000 |
| Lloyds | 4,425 |
| Lloyds Banking Group Total | 7,425 |
| Royal Bank of Scotland | 1,007 |
| RBS Banking Group Total | 1,007 |
| Goldman Sachs | 8,000 |
| Standard Chartered | 2,000 |
| Santander | 4,604 |
| Barclays Bank Plc | 1 |
| Svenska Handelsbanken | 1,500 |
| UBS | 2,000 |
| Rabobank | 2,000 |
| Other Banks Total | 20,105 |
| TOTAL INVESTMENTS | <u>£30,439</u> |
| Local Authority | 2,000 |
| PWLB | 104,717 |
| TOTAL BORROWING | <u>£106,717</u> |

Borrowing

13. The Council's revised Capital Financing Requirements (CFR) for 2017/18 is £113.984m. The CFR denotes the Council's underlying need to borrow for capital purposes. If the CFR is positive the Council may borrow from the PWLB or the market (External Borrowing) or from internal balances on a temporary basis (Internal Borrowing). The Council has external borrowing of £106,717m as at 30 June 2017, as well as a further £4.740m of internal borrowing.

Compliance with Treasury and Prudential Limits

14. It is a statutory duty for the Council to determine and keep under review the “Affordable Borrowing Limits”. Council’s approved Treasury and Prudential Indicators are outlined in the approved TMSS.
15. During the period to 30 June 2017 the Council has operated within treasury limits and Prudential Indicators set out in the Council’s TMSS and with the Council’s Treasury Management Practices. The Prudential and Treasury Indicators are shown in Appendix B.

Early Payment of Pension Lump Sums

16. The Council agreed with the Pension Fund to pay 3 years’ pension lump sums in 4 instalments (Apr, Jul, Oct & Jan) during 2017-18. The cash value of these prepayments is £6.497m, rather than £6.809m if paid annually over 3 years, a cash saving of £312k. An estimated £50k of interest will be foregone.

Local Authority Mortgage Scheme (LAMS) Financial Guarantee Outstanding

17. Whilst the £1m investment has been repaid (see paragraph 9) the LAMS financial guarantee will reduce gradually as each individual mortgage reaches the 5 year mark. At this point, if the mortgage has been in arrears during the previous 6 months the financial guarantee will be extended for a further 2 years. Table 3 below shows the current maximum liability, and how it is scheduled to diminish. It is worth noting that to date none of the 37 loans have been in arrears during the period of the scheme.

Table 3: Outstanding LAMS Financial Guarantee

| Month | £'000 |
|--------------|--------------|
| Sep-17 | 799 |
| Dec-17 | 536 |
| Mar-18 | 494 |
| Jun-18 | 412 |
| Sep-18 | 330 |
| Dec-18 | 84 |
| Mar-19 | 53 |
| Jun-19 | 53 |
| Sep-19 | 25 |
| Dec-19 | 25 |
| Mar-20 | 25 |
| Jun-20 | 25 |
| Sep-20 | 0 |

Economic Background

UK data has been less robust in recent months and, in particular, all of the June Purchasing Manager Index (PMI) numbers turned lower, while consumer confidence dipped to its lowest level since the EU referendum. Household savings levels are at a record low, though there may be some temporary influences, and that raises doubts over the maintaining of Q1's already subdued household spending growth. The composite PMI is, though, reflective of 0.5% q/q growth in Q2, a level also indicated by the CBI's growth tracker. The largest drag on the economy in Q1 was the retail sector and there appears to have been a partial reversal of the declines in Q2. Overall, economists still expect a bounce in quarterly growth to around 0.5%.

EZ consumer price inflation eased to 1.3% y/y in June but the core rate increased to 1.1%, which is markedly higher than the average over the last two and a half years. This indicates that underlying price pressures may be on the rise. Looking from a national perspective, however, it looks like this pick up is being driven almost exclusively by Germany, with other economies seeing subdued pressures as slack remains a feature of the economy. High unemployment and low interest rate expectations in other areas should ensure that price pressure (excluding Germany) remains weak.

Recent economic releases back the view that the US economy is following the pattern of recent years ... weak Q1, improving in Q2. Indeed, the latest figures point to growth surging to near 3% annualised in Q2 on real consumption growth. Underlying retail sales eased in May but previous strength saw the q/q annualised growth hit an 11 month high of 5.1%. Labour market conditions also continue to be healthy, with real income growth improving and consumer confidence at elevated levels. Analysts suggest these factors should help to boost real consumption to annualised growth of 2.5% for the remainder of the year.

The two leading Asian economies seem to be heading in slightly different directions. There is ongoing evidence that the Chinese economy is still experiencing some slowing, though buoyant external demand should underpin growth levels. Meanwhile, Japanese economic recovery is continuing, and though largely driven by export growth, there is evidence that domestic consumer spending is strengthening as employment conditions continue to improve. The lack of price pressures does suggest that private consumption levels have further to go.

UK

Q1 was confirmed as having experienced a sharp slowing in the rate of growth to 0.2% q/q, from 0.7% the previous quarter. Households are feeling the effect of rising inflation on spending capacity so the 0.4% q/q increase in consumer spending looks likely to weaken, as growth was supported by savings levels being cut to a record low. The decline in the savings ratio was in part due to temporary factors, but higher tax payments also hit disposable income. Elsewhere, output indices reflect an increased pace through Q1, which extended into Q2. Overall, analysts see Q1's tepid performance as a blip rather than an on-going problem.

Consumer spending growth slowed to 0.4% in Q1 on weaker retail spending but the sector is having a better Q2. If sales volumes held steady in June that would see strong quarterly growth of 1.2%. However, real household disposable income fell 1.4% q/q in Q1, which indicates less saving and increased borrowing. This was also evidenced by unsecured credit growth running at around 10% y/y. Though the saving ratio fell to a record low, confidence levels suggest that credit growth is set to continue.

Sterling's weakening has, to date, had little positive impact on the external sector, with net trade a drag on Q1 GDP growth, as imports grew at more than double the pace of exports. The volatile "valuables" component was the cause of most of the weakness over the quarter. The trade balance has improved little since the start of Sterling's decline, but the investment income deficit has narrowed markedly since Brexit. Indeed, the weak net trade performance has been put down to strong imports growth, for both goods and tourism services. But import growth has started to ease in recent months and surveys point to improved export prospects, both from a price and capacity perspective.

Employment growth picked up in the three months to April but the annual rate of growth was unchanged at 1.2%, as was the unemployment rate of 4.6%. Hiring intentions point to sustained growth in the short term but rising inflation and muted wage growth will increase pressure on real wages, with "real" annual wage growth (i.e. taking account of underlying inflation) slipping to -0.9% in April. Given the tightness of the labour market this is remarkable, but there has been a decline in hourly productivity levels in Q1 and weakness of productivity growth will restrict higher pay awards.

CPI increased to 2.9% in May, the highest since 2013 as falling fuel prices were outweighed by gains in other areas. The pick-up in recent months is down to the import intensive areas of the basket of goods used to measure price changes. On the positive side, wholesale energy prices have receded, which will soften pressures on households if suppliers pass on cheaper costs, while food price inflation may be near its peak if historical correlations between domestic producer and imported food price inflation hold. The full Sterling impact may not be too far away but front end pipeline pressures are also easing, and higher household inflation expectations do not seem to be becoming entrenched. Domestic inflation has levelled off recently and it should be noted that not all inflation can be put down to Brexit as other economies have seen headline inflation increase too. Analysts are looking for CPI to peak around in the autumn before edging slowly back toward target. As rent growth has been stronger than that seen in other consumer sectors, CPIH (the BoE's preferred indicator) is likely to exceed CPI, while the spread between RPI and CPI should continue to narrow as house price inflation slows further.

EZ

The EZ economy has generated some momentum and GDP growth should accelerate in Q2, though the pace of expansion may slow later in the year. Q1 growth was revised higher to 0.6% q/q, which is the strongest for two years, with domestic demand leading the recovery and investment also a strong contributor. Softer industrial production figures in April were disappointing but May consumer spending has made up for that and led to stronger growth in Q2. Surveys have been

upbeat, with the EC Economic Sentiment Indicator hitting a near ten year high, which equates to annual GDP growth rising to 2.5% and a quarterly gain of 0.8%. Though the composite PMI is slightly less buoyant, falling in June, it also reflects a further rise in quarterly growth in Q2. At a national level, though, there is some divergence between members and the future output and new orders indices of the composite PMI offer an indication of growth slowing in the coming months.

Consumer spending grew 0.3% in Q1, the slowest rate for eleven quarters, pulling the annual rate of growth lower. However, the sector has had a positive start to Q2, and surveys indicate very healthy growth to come. Retail sales grew for a fifth month, rising in all of the major economies, led by France. Sales volumes have been hit by rising inflation but values have remained strong. Inflation is, though, starting to ease. There was a sharp improvement in consumer confidence in June, to a 74 month high, which should bode well for future spending growth. The bloc wide level was boosted by the gain in France, which posted one of the highest monthly gains in the index's history, as consumer confidence there nears record highs.

Industry had a weak Q1, but more recent indicators suggest an improvement in Q2. The sector grew by just 0.2% in Q1, but this was signalled by data over the quarter. Production rose 0.5% m/m in April which offers a positive opening to Q2. The manufacturing PMI made further gains in June, posting a 75 month high to be consistent with annual production growth increasing to 4.5%. The EC sentiment indicator for services also improved but suggests that Q2 output growth in the sector will be unchanged at 1.9%.

Q1 EZ GDP growth was held back by net exports but the outlook is more promising according to indicators. Goods and services trade added little to quarterly GDP in Q1 but impacted negatively on the annual rate. The April nominal goods and services trade surplus narrowed further. The net trade drag is down to import strength, rather than weak exports, indeed the value growth in the latter cannot be put down to exchange rate movements alone. Export volumes have been boosted by improved world trade, as well as healthy global GDP growth and the manufacturing PMI export orders index points to acceleration in volume growth in the coming months.

The labour market has seen recovery slow markedly with unemployment falling by just 16,000 in May, with the decline from April entirely down to volatility in Italy. The overall unemployment rate was unchanged at 9.3% but Italy saw a rise in its rate. The surveys suggest that the slowing was temporary with hiring intentions consistent with annualised employment growth around the 1.5% seen in Q1. The continued recovery should offer potential for wage growth, which on previous form would see increases of more than 2% by year end.

Though core inflation increased in some member countries, headline EZ inflation softened to 1.3% in June, as falling oil prices eased energy inflation. Core inflation picked up to 1.1%, but was this the effect of a bank holiday in Germany as elsewhere it remains relatively weak? Forecasts for the oil price and the value of the Euro indicate energy inflation being broadly stable but core inflation may tick higher given falling unemployment and increased inflation expectations. Consumer goods PPI, excluding food and energy, was, however, unchanged in May to indicate little in

the way of pipeline pressures. Inflation in individual member states will remain divergent with Germany already operating beyond capacity, which should imply rising price pressures, whereas the other major economies are still operating with output gaps, and subdued inflation.

Markets were shaken by comments from Mario Draghi at the end of the month, which were seen as hawkish, resulting in a tightening of the interest rate hike probability to June 2018, leaving bond yields higher across the board. Greece was the main exception as yields fell on creditors agreeing to pay the next tranche of bailout funds. While relative interest rates were unchanged, the Euro strengthened against the US\$ on Draghi's speech, indicating that investors outlook for unconventional monetary policy has also changed. Equities did not respond well to the stronger currency, but remain in line with economic sentiment levels. However, they probably would have been lower were it not for the bailout of two regional Italian banks.

US

Q1 growth was weak but, as has been the case in recent years, the outlook for Q2 is rather stronger, with annualised growth looking to jump from 1.2% to 3%, as the ISM surveys remain high and indicative of improved growth. In particular, stronger global growth and a weaker Dollar point to better times ahead than there have been for a while. Indeed, small business sentiment remains very strong having hit long time highs in the wake of the Presidential election.

Consumption showed some recovery in March, after a difficult start to the year, and April was also a positive month. Retail sales figures reflect strong underlying sales, with core sales growing at around 5% y/y. Weak new vehicle sales, though, will weigh on consumption growth, a consequence of a mass of ex-lease vehicles undermining used car prices and tighter auto-loan conditions. The pace of auto sales declines will be maintained at Q1 levels and other forms of credit seem unrestricted. Fundamentals remain strong, with real disposable incomes increasing again and consumer confidence levels very high, and consistent with strong consumption growth.

The pickup in drilling activity could be threatened by falling crude oil prices. Having surged by 460% annualised in Q1, mining investment is likely to be more restrained for the remainder of the year. However, business investment prospects are better with orders and shipments of capital goods bouncing strongly in the last year. Survey capex intentions are markedly higher than through the last two years and, while commercial and industrial loans have been weak, corporate bond issuance is higher this year resultant from fresh declines in bond yields. Housing starts have dropped which seems strange given low inventory levels, but this suggests weak residential investment levels in Q2. Construction spending data is more positive, so after declining in Q1 government investment should level off.

There has been a widening of the trade deficit but it is not much above the average of recent years. The April increase was the result of stronger imports combining with lower exports, thus net trade is set to be a drag on annualised Q2 GDP growth. Analysts are looking for export growth to accelerate as the impact of the Dollar appreciation has faded and a recent weaker Dollar should help export growth.

Surveys are encouraging, indicating real exports might expanded at 8% y/y, largely on improvements in the Eurozone. Imports may also increase, though increased domestic crude oil output should see imports level off.

The weak non-farm payroll gain of 138,000 in May is a continuation of broader slower growth in recent years. The recent weakening of job creation has come in the low wage sectors and retail in particular, though this does point to the overall mix of new jobs being improved. Slower employment gains have, though, continued to pull the unemployment rate down, with the May rate of 4.3% a 16 year low. Survey indications are that the rate could dip below 4% in the months ahead, but that may prove a bit too upbeat. The strength of the labour market has drawn prime working age people back into the workforce in greater numbers and that growth in activity of 25-54 year olds should put pressure on wages at some point.

The CPI measure of inflation has fallen back to 1.9% from a five year high 2.7% earlier in the year, largely on declining energy prices, a situation that should not persist. Core inflation, though, has slowed markedly to 1.7% in May, with the three month annualised rate at a seven year low 0%. Weakness at the core has been broad but exacerbated by steep declines in specific areas, such as medical care. As noted earlier, the large number of former lease vehicles coming to market has weighed on auto prices and with the vehicle pipeline set to rise there could be further deflationary pressures brought to the market. The core PCE inflation level (the Fed's measure of choice) is little changed, but is weaker, though there are reasons why CPI should bounce soon. There have been no indications of weakness in producer prices, with core PPI hitting a three year high in May. The PPI consumer services pickup points to a similar move in PCE services, while the US \$ is no longer having a dampening effect on import prices, thus core goods inflation may start to increase. Inflation compensation has eased recently, but they remain low. Meanwhile, survey based measures of consumer inflation expectations are starting to bounce.

The Fed raised interest rates again in June and reiterated that the intention is for gradual tightening. However, markets are still only looking for another 25 basis points increase by the end of next year, while the 10 year Treasury bond yield has actually fallen. The flattening of the yield curve is seen as a bearish signal for the economy by some. Dollar weakening has continued with the Fed's trade weighted dollar index having reversed its previous surge, post-election. The stock market has taken the Fed's tightening programme in its stride so far, and Wall Street sees indices hitting record highs. But there are still concerns about the lack of policy delivery from the Trump administration.

Asia

The Chinese activity indicators are hinting at a further deceleration in May. Investment growth continued to slow in nominal terms, but this was largely due to pricing effects, and in real terms was stable. State led infrastructure spending has underpinned investment, though even this has slowed over the last year. Consumer indicators point to weak auto sales, but the labour market remained healthy in Q1, though there have been recent signs of conditions weakening. Business indicators have also highlighted some slowing, with conditions for larger companies deteriorating. However, this has been offset by a sharp improvement in conditions

for small and medium sized firms. External indicators suggest that external demand has held up well and is buoyant, with the trade surplus widening further in May. Chinese inflation has picked up in the last three months, after the sharp fall in February, led by a pick-up in food price inflation. The People's Bank of China has been pushing market interest rates higher since last October but analysts believe that the tightening cycle is now at an end. The ebbs and flows in the Chinese economy are largely masked by official data releases that smooth out these movements. While this does distort the month by month picture of the economy the overall annual performance tends to be truly reflected, and in 2017 analysts believe that the economy will just about meet target levels, or fall just shy of them.

The Japanese economy has been helped by a surge in exports but there is evidence that domestic consumption is also starting to play a role, with spending looking to be in line for another strong quarterly pick up in Q2. Output and activity has seen the economy grow for a fifth successive quarter in Q1. There has been some moderation in export growth but the rise in industrial production indicates that momentum has been maintained into Q2. Consumption seems to be picking up on broad increases in goods and services activity and households seem upbeat, which could result in a dip in the savings rate. With corporate profits hitting record highs and firms having strong balance sheets, the business indicators are suggesting further solid gains in economic activity. Job growth remained strong and there are rising numbers of jobs available, but wage growth is still subdued. It appears that higher energy prices are putting upside pressures on inflation, but despite expectations that underlying inflation will start to pick up as well analysts do not see price pressures strengthening much more. The Bank of Japan has continued to ease back on its bond purchasing programme, while a stronger Yen has not prevented the Nikkei hitting fresh highs. Nevertheless, equities are looking to be fully valued and have limited upside.

Summary

Politics is playing an increasingly influential role in the state of the markets at present. In the UK there has been a sense of mounting turmoil in the wake of the lack of a clear mandate for the ruling Conservative party at the General Election. With Brexit negotiations starting for real there is a sense of divide among Mrs May's Cabinet, which threatens to add to the uncertainty, while there appears to be no clear plan for withdrawal. Constant speculation about the length of Mrs May's tenure at Number 10 does not help matters. At the end of the month the Bank of England seemed to take a more hawkish stance, raising speculation of an earlier than expected rate hike. However, against a background of political uncertainty, very mixed economic data and a workforce seeing real wages in decline, it seems that a hike sometime soon is a bit fanciful.

Meanwhile in the US, Donald Trump continues to make waves. Amidst all of his squabbles with the press and noise surrounding his campaign team's involvement, or not, with the Russians, more concerning is that there has been no great progress on his political agenda which won him the election. Never mind the President's first 100 days it may be a case of the first 100 delays and the possibility is that the first year of his White House occupation could deliver little or nothing of note.

Markets

| | Open | Close | High | Low |
|----------|----------|----------|----------|----------|
| FTSE 100 | 7,520 | 7,313 | 7,561 | 7,303 |
| £/\$ | \$1.2887 | \$1.3025 | \$1.3030 | \$1.2587 |
| €/£ | £0.8721 | £0.8769 | £0.8846 | £0.8649 |
| 5y Gilt | 0.486% | 0.697% | 0.728% | 0.354% |
| 10y Gilt | 1.049% | 1.259% | 1.292% | 0.928% |
| 25y Gilt | 1.711% | 1.877% | 1.913% | 1.641% |
| 50y Gilt | 1.539% | 1.693% | 1.728% | 1.468% |

The General Election result saw markets react to the Government's loss of an absolute majority, which leaves it reliant on an agreement with the Irish Democratic Unionist Party.

Sterling slipped to a 3 month low on a trade weighted basis, but recent, end of month hawkish MPC comments have seen a bounce. This has left the currency only marginally lower against the €uro and the US\$.

That change in MPC mood has seen markets pull expectation of the first 0.25% rate hike in to Q2 2018, which is a year earlier than had been priced in a month or so ago. As a consequence there was a sharp firming in gilt yields at the close of the month.

Equities have underperformed compared to those elsewhere as the election outcome has weighed on investor sentiment. Firms with a more domestic lien on income have fared worse than the more internationally engaged.

Prudential Indicators as at June 2017

| Prudential Indicator | 2017/18 Indicator £'000 | Actual as at 30 June 2017 £'000 |
|--|-------------------------------|---------------------------------------|
| Capital Financing Requirement (CFR) | 113,984 | 112,089 |
| Gross Borrowing | 107,717 | 106,717 |
| Authorised Limit for external debt | 128,000 | 106,717 |
| Operational Boundary for external debt | 120,000 | 106,717 |
| Limit of fixed interest rates based on net debt | 100% | 100% |
| Limit of variable interest rates based on net debt | 25% | 0% |
| Principal sums invested > 364 days | 8,000 | 0 |
| Maturity structure of borrowing limits | | |
| Under 12 months | 25% | 1% |
| 12 months to 2 years | 50% | 2% |
| 2 years to 5 years | 75% | 1% |
| 5 years to 10 years | 100% | 2% |
| 10 years and above | 100% | 94% |

Explanation of prudential indicators

Central Government control of borrowing was ended and replaced with Prudential borrowing by the Local Government Act 2003. Prudential borrowing permitted local government organisations to borrow to fund capital spending plans provided they could demonstrate their affordability. Prudential indicators are the means to demonstrate affordability.

Gross borrowing – compares estimated gross borrowing in February 2017 strategy with actual gross borrowing as at 30 June 2017.

Capital financing requirement (CFR) – the capital financing requirement shows the underlying need of the Council to borrow for capital purposes as determined from the balance sheet. The overall positive CFR of £113,984m provides the Council with the opportunity to borrow if appropriate. No external borrowing is planned for 2017/18.

Authorised limit for external debt - this is the maximum limit for gross external indebtedness. This is the statutory limit determined under section 3(1) of the Local Government Act 2003. This limit is set to allow sufficient headroom for day to day operational management of cashflows. This limit has not been breached in the period 1 April 2017 to 30 June 2017.

Operational boundary for external debt – this is set as the more likely amount that may be required for day to day cashflow. This limit has not been breached in the period 1 April 2017 to 30 June 2017.

Upper limit for fixed and variable interest rate exposure – these limits allow the Council flexibility in its investment and borrowing options. Current investments are either fixed rate term investments or on call. Borrowing is at a fixed rate.

Upper limit for total principal sums invested for over 364 days – the amount it is considered can prudently be invested for a period in excess of a year. Current policy only permits lending beyond 1 year with other Local Authorities up to a maximum of 3 years, apart from the £1m invested until the 24th April 2017 for 5 years as part of the Local Area Mortgage Scheme.