To all Members of the Audit and Standards Committee

A meeting of the **Audit and Standards Committee** will be held in the **Ditchling Room, Southover House, Southover Road, Lewes Southover House, Southover Road, Lewes** on **Monday, 16 January 2017** at **10:00** which you are requested to attend.

Please note the venue for this meeting which is wheelchair accessible and has an induction loop to help people who are hearing impaired.

This meeting may be filmed, recorded or broadcast by any person or organisation. Anyone wishing to film or record must notify the Chair prior to the start of the meeting. Members of the public attending the meeting are deemed to have consented to be filmed or recorded, as liability for this is not within the Council's control.

06/01/2017

Catherine Knight
Assistant Director of Legal and Democratic Services

Agenda

1 **Minutes**
To approve the Minutes of the meeting held on 28 November 2016 (copy previously circulated).

2 **Apologies for Absence/Declaration of Substitute Members**

3 **Declarations of Interest**
Disclosure by councillors of personal interests in matters on the agenda, the nature of any interest and whether the councillor regards the interest as prejudicial under the terms of the Code of Conduct.

4 **Urgent Items**
Items not on the agenda which the Chair of the meeting is of the opinion should be considered as a matter of urgency by reason of special circumstances as defined in Section 100B(4)(b) of the Local Government Act 1972.

5 **Written Questions**
To deal with written questions from councillors pursuant to Council Procedure Rule 12.3 (page D8 of the Constitution).

6 **Interim Report on the Council's Systems of Internal Control 2016/17 (page 3)**
To receive the Report of the Head of Audit, Fraud and Procurement (Report No 13/17 herewith)

7 **Oversight of the Council's Surveillance Policy (page 15)**
To receive the Report of the Assistant Director of Legal & Democratic Services (Report No 14/17 herewith)

8 **Treasury Management (page 21)**
To consider the Report of the Deputy Chief Executive (Report No 15/17 herewith)

9 **Annual Treasury Management Strategy Statement and Investment Strategy 2017/2018 to 2019/2020 (page 26)**
To consider the Report of the Deputy Chief Executive (Report No 16/17 herewith)

10 **Date of Next Meeting**
To note that the next meeting of the Audit and Standards Committee is scheduled to be held on Monday, 20 March 2017 in the Ditchling Room, Southover House, Southover Road, Lewes commencing at 10.00am.

For further information about items appearing on this Agenda, please contact Zoe Downton at Southover House, Southover Road, Lewes, East Sussex BN7 1AB Telephone 01273 471600

Distribution: Councillors M Chartier (Chair), S Catlin, N Enever, S Gauntlett, I Linington, R Robertson and T Rowell

(Members of the Committee who are unable to attend this meeting or find a substitute councillor to attend on their behalf should notify Zoe Downton, Committee Officer, zoe.downton@lewes.gov.uk)

Agenda Item No:	**6**	**Report No:**	**13/17**
Report Title:	**Interim Report on the Council's Systems of Internal Control 2016/17**		
Report To:	**Audit and Standards Committee**	**Date: 16 January 2017**	
Ward(s) Affected:	**All**		
Report By:	**Head of Audit, Fraud and Procurement**		

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Purpose of Report:

To inform Councillors on the adequacy and effectiveness of the Council's systems of internal control during the first eight months of 2016/17, and to summarise the work on which this opinion is based.

Officers Recommendation(s):

1 To note that the overall standards of internal control were satisfactory during the first eight months of 2016/17 (as shown in Section 3).

Reasons for Recommendations

1 The remit of the Audit and Standards Committee includes the duties to agree an Annual Audit Plan and keep it under review, and to keep under review the probity and effectiveness of internal controls, both financial and operational, including the Council's arrangements for identifying and managing risk.

Information

2 Background

2.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) has, with the other governing bodies that set auditing standards for the various parts of the public sector, adopted a common set of Public Sector Internal Audit Standards (PSIAS) that were applied from 1 April 2013. The Head of Audit, Fraud and Procurement (HAFP) advised the Audit and Standards Committee of the effect of the standards at its March 2013 meeting.

2.2 The PSIAS have been updated, with new standards published in April 2016. The impact of the new standards was reported to the September 2016 meeting of the Committee.

2.3 The PSIAS 2016 continue to specify the requirements for the reporting to the Audit and Standards Committee and senior management by HAFP. These requirements are met via a series of reports, including interim reports to each meeting of the Committee.

2.4 Each interim report includes a review of the work undertaken by Internal Audit compared to the annual programme, an opinion of HAFP on the internal control, risk management and governance environment at the Council, together with any significant risk exposures and control issues, in the period since the beginning of the financial year. Each interim report contains an appendix that includes an outline of each of the final audit reports issued since the previous meeting of the Committee, and an appendix that outlines any significant recommendations that have not yet been implemented.

3 Internal Control Environment at Lewes District Council

3.1 The Annual Report on the Council's Systems of Internal Control for 2015/16 included the opinion of HAFP that the overall standards of internal control are satisfactory. This opinion was based on the work of Internal Audit and the Council's external auditors, BDO, and the Council's work on risk management. In the eight months since the start of the financial year there has been nothing to cause that opinion to change and there have been no instances in which internal control issues created significant risks for Council activities or services. Prompt corrective action was taken to address issues noted during an internal audit of the Council's Right to Buy (RTB) processes (see also 4.8).

4 Internal Audit work 2016/17

4.1 This section of the report summarises the work undertaken by Internal Audit during the first eight months of the year, compared to the annual plan that was presented to the Audit and Standards Committee in March 2016. Further information on each of the audits completed since the previous meeting of the Committee is given at Appendix A.

4.2 Table 1 shows that a total of 462 audit days have been undertaken compared to 427 planned.

Table 1: Plan audit days compared to actual audit days for April to November 2016

Audit Area	Actual audit days for the year 2015/16	Plan audit days for the year 2016/17	Actual audit days to date	Pro rata plan audit days to date
Main Systems	360	290	222	
Central Systems	57	70	79	
Departmental Systems	68	70	83	
Performance and Management Scrutiny	27	45	8	
Computer Audit	2	45	-	
Management Responsibilities/Unplanned Audits	88	116	70	
Total	602	636	462	427

Note: The 'Pro rata plan audit days to date' provides a broad guide to the resources required to carry out planned audits. The actual timing of the individual audits will depend on a variety of factors, including the workloads and other commitments in the departments to be audited.

4.3 The variance of 35 days has largely been due to the Head of Audit, Fraud and Procurement being involved in more direct audit work at this stage of the year than was originally envisaged. It is estimated that the audit days will be close to plan by the year end, partly because of the staff change outlined at 4.4 below.

4.4 One of the Senior Auditors at LDC has confirmed his planned retirement in January 2017. The intention is for the vacancy to be filled at Auditor level, although the recruitment process is in its early stages and, depending on the outcome, there could be a reduction in the days available for audit work in the latter months of 2016/17.

4.5 ***Main Systems:*** The initial work was on the testing of the major financial systems in order to gain assurance on the adequacy of internal controls for the Annual Governance Statement (AGS) and to inform BDO's work on the Council's accounts for 2015/16. A final report has been issued.

4.6 The work on behalf of BDO to test the Council's subsidy claims for Benefits for 2015/16 is underway. BDO's initial planning for this work had set out the standard testing requirements and identified the likely need for significant additional testing to address the issues noted in the previous year's claim. The standard testing was completed, and the test samples for the additional testing were confirmed in late October. The additional testing has been underway since then but the claim was not submitted to the Department of Work and Pensions (DWP) by the normal submission date at the end of November 2016. The Benefits subsidy claim is the priority task for Internal Audit.

4.7 ***Central Systems:*** Some outstanding issues from the audit of Electoral Registration and Elections are being examined prior to confirmation of the draft report. Final reports have been issued for the audit of Ethics, Newhaven Business Centre, Insurance, and for the priority audit of Business Continuity Planning (BCP). The results of the joint review of the EBC/LDC Leisure Trusts have been discussed with CMT, and the final version of the report will be issued shortly.

4.8 ***Departmental Systems:*** The final reports from the audits of Right to Buy (RTB), Private Sector Housing and Cemeteries have been issued. The audit of Estates Management, incorporating work on the corresponding function at EBC, has been planned and will commence in January 2017.

4.9 The final report from the audit of RTB included an estimate of the impact of the discounting errors in completed and ongoing RTB sales in the period 2012/13 – 2015/16. The estimated loss to LDC was approximately £100,000. Immediate action was taken to correct the prices of ongoing sales, as was reported to the September 2016 meeting of the Committee. The effect is that the loss to LDC has been reduced to £88,000.

4.10 ***Performance and Management Scrutiny:*** The main work in this category has been in reviewing the data that supports the Annual Governance Statement (AGS), and specific tasks related to the Internal Audit aspects of the Council's Joint Transformation Programme (JTP).

4.11 ***Computer Audit:*** Internal Audit has examined the IT aspects of the main financial systems (see 4.5 above).

4.12 ***Management Responsibilities/Unplanned Audits:*** This category provides resources for activities such as support for the Audit and Standards Committee, managing the Fraud Investigations Team, liaison with BDO, and managing the Follow Up procedures. There has been just one unplanned audit - a small scale exercise to review cash handling procedures at the Lewes Tourist Information Centre, and there were no significant outcomes.

5 Follow up of Audit Recommendations

5.1 All audit recommendations are followed up to determine whether control issues noted by the original audits have been resolved. The early focus for follow up in 2016/17 was on confirming the implementation of the recommendations that had been agreed in the previous year. The results of this work were reported separately to the June 2016 meeting of the Committee.

6 Quality Reviews/Customer Satisfaction Surveys/Performance Indicators (PIs)

6.1 The results of the Internal Audit quality reviews, customer satisfaction surveys and PIs for 2015/16, and the targets for 2016/17, were reported to the June 2016 meeting of the Committee. The results enabled the HAFP to report that the Internal Audit service at Lewes is fully effective, is subject to satisfactory management oversight, achieves its aims, and objectives, and operates in accordance with the Internal Audit Strategy as approved by the Committee.

7 Review of 2016/17 Audit Plan

7.1 As part of the report to the March 2016 meeting of the Committee that detailed the Annual Audit Plan, HAFP advised that there would be a nine month review of the Audit Plan for 2016/17 to assess whether any significant changes are necessary.

7.2 That review will take place at the nine month stage and the results of the review will be presented to the Committee. As an interim measure HAFP advises that, with the current rate of progress, all significant aspects of the annual audit plan will be covered. The only exception is the planned audit of IT Security and Networks that will not be possible because of the retirement of the Senior Auditor who is the specialist computer auditor.

8 Combatting Fraud and Corruption

8.1 The Annual Report on the Council's work to combat Fraud and Corruption 2015/16 was presented to the June 2016 meeting of the Committee. That report was a detailed statement of the strategies and structures that in place to counter fraud and corruption, and the information within the report is still accurate and relevant. Below are updates that outline the main developments since the start of 2016/17.

Local developments

8.2 The Investigation Team maintains its membership of the East Sussex Fraud Officers Group (ESFOG), a body that enables information sharing and joint initiatives with neighbouring authorities on a wide range of counter fraud work. A sub group of six authorities within ESFOG are working together in a 'Hub' approach to coordinate new anti-fraud initiatives across East Sussex and Brighton.

8.3 The Hub has funded training, the implementation of a shared case management system, a housing support system that enables the analysis of tenancy data to help improve tenancy management and highlight fraud risks, and a programme of counter fraud publicity work by the private sector company PRG.

LDC Investigations Team

8.4 The Council has in place an agreement with DWP for the management of cases of HB fraud, and officers work with local DWP teams to help ensure efficient operation of the processes covered by the agreement. The major work on each case is the responsibility of the national Single Fraud Investigation Service (SFIS) within DWP. The Council retains a role in referring cases of suspected HB fraud to SFIS and handling requests for information. In an agreement with the Investigation Team at EBC a member of that team has, since mid-August 2016, taken over the Council's SFIS liaison work. Since 1 April 2016, 87 HB cases have been passed to SFIS, and 56 information requests have been actioned.

8.5 The LDC Investigations Team retains responsibility for dealing with the cases of suspected Council Tax Reduction Scheme (CTRS) fraud that are often linked to HB cases, and administering the penalties for cases that are not subject to prosecution. Nine cases are currently under review and one case is being investigated.

8.6 The main focus of the team's work in 2016/17 has been in continuing to address tenancy issues. The team's approach has included obtaining best practice guidance from other authorities, and maintaining effective referral arrangements with officers in LDC Housing Services. Two properties have been returned to the Council's housing stock, and another property return will take place during January 2017. A further 18 suspected cases of abandonment or subletting are being investigated or are undergoing pre-investigation review.

8.7 Since July 2016, the Investigation Team has been operating a new regime of checks on Right to Buy (RTB) applications to prevent and detect fraud, and protect the Council against money laundering. To date, 18 RTB applications have been withdrawn after intervention by the Investigations Team. The team has been examining the withdrawn applications and one of the ongoing applications because some of the cases indicate potential fraud; three investigations are underway.

National Fraud Initiative (NFI)

8.8 Internal Audit continues to coordinate the Council's work on NFI data matching exercises. Council services submitted the various data ranges in mid-October 2016 and have dealt with a number of queries since then.

8.9 Internal Audit, the Investigations Team and service managers are preparing for the receipt of the reported matches in February 2017. New types of matches, and forecasts of more matches in categories such as Identity Theft, mean that the Investigations Team will have a greater role than previously in dealing with output from the exercise. Future reports to the Committee will contain progress reports on the NFI.

9 Risk Management

9.1 Cabinet approved the Risk Management Strategy in September 2003. Since then risk management at the Council has been the subject of ongoing development, with the result that all the elements of the risk management framework set out in the strategy are in place and are maintained at best practice standards.

9.2 The risk management process has identified that most risks are mitigated by the effective operation of controls or other measures. However, there are some risks that are beyond its control, for example a major incident, a ‘flu’ pandemic, a downturn in the national economy or a major change in government policy or legislation. The Council has sound planning and response measures to mitigate the effects of such events, and continues to monitor risks and the effectiveness of controls. The overall satisfactory situation for risk management has helped to inform the opinion on the internal control environment.

10 The Government introduced a national deficit reduction plan for the public sector in 2011/12. In response, the Council has committed to a phased annual programme to make budget savings. The total value of savings made in the General Fund budget (which covers all services except the management and maintenance of Council-owned homes) since 2011/12 has been £3.5m with each annual savings target being successfully achieved in-year.

11 When setting the General Fund budget for 2016/17, the Council identified a requirement to make further savings, which will reduce spending by £2.8m over the four years to 2019/20. The target for 2016/17 is £685,000 of which £400,000 is to be generated from the JTP with EBC. A budget has been allocated to finance the investment needed to implement the changes required through the JTP

12 There are also pressures to reduce spending on the management and maintenance of Council owned (HRA) housing. The Government has introduced a number of measures, starting in 2016/17, which will reduce the amount of income that it receives from tenants. The first of these measures, a 1% annual reduction in tenants’ rents for each of the next four years, will incrementally reduce HRA income by £2.8m by 2019/20, the total shortfall in that period being £6.9m.

12.1 The Annual Report on Risk Management was presented to the June 2016 meeting of the Committee. The report forms part of the annual reporting cycle on risk as set out in the Risk Management Strategy. The report was presented to Cabinet at its July 2016 meeting.

13 System of management assurance

13.1 The Council operates a management assurance system, which enabled senior officers to confirm the proper operation of internal controls, including compliance with the Constitution, in those services for which they are responsible. As part of this process all members of the Corporate Management Team (CMT) are required to consider whether there were any significant governance issues during 2015/16. At its meeting on 3 May 2016 CMT confirmed that there were no significant governance issues to report. There has been nothing in the first eight months of the financial year to change these assessments.

14 Corporate governance

14.1 In March 2016, HAFP reviewed the Council’s Local Code of Corporate Governance, and concluded that the arrangements remain satisfactory and fit for purpose. These results were reported to the March 2016 meeting of the Committee.

14.2 The Council is required to produce an Annual Governance Statement (AGS), which outlines the main elements of the Council's governance arrangements and the results of the annual review of the governance framework including the system of internal control. The draft AGS for 2016 was presented to the June 2016 meeting of the Committee, and the final version of the AGS was presented to the September 2016 meeting of the Committee with the Statement of Accounts for 2015/16.

15 External assurance

15.1 The Government relies on external auditors to periodically review the work of the Council to make sure it is meeting its statutory obligations and performing well in its services. The results of these external reviews have helped inform the opinion on the internal control environment. The recent results are summarised below.

15.2 Annual Audit Letter for 2015/16 (October 2016) – This report summarises the key issues from the work carried out by BDO during the year, and was presented to the November 2016 meeting of the Committee. The key issues were:

- BDO issued an unqualified true and fair opinion on the financial statements for the period ended 31 March 2016.
- BDO identified a number of misstatements on the Cash Flow Statement and in the classification of short term investments. These were corrected before completion of the financial statements.
- BDO were satisfied that the Narrative Report, which local authorities include in the Statement of Accounts to offer interested parties guidance on the most significant matters, was consistent with the financial statements.
- BDO did not identify any significant deficiencies in the Council's framework of internal controls, but did report on areas where improvements in controls could be made including declarations of related party transactions, the documentation of Council Tax discounts, and access to some IT systems.
- BDO were satisfied that the Annual Governance Statement (AGS) was not misleading or inconsistent with other information they were aware of from their audit work.
- BDO issued an unqualified conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources.
- BDO found that the Council has adequate arrangements for budget setting and budget monitoring, and the Council has identified sufficient savings over the next four years to balance its budget.
- BDO noted that many of the savings will arise from the Joint Transformation Programme with EBC, and BDO were satisfied that there are effective governance arrangements in place to oversee delivery of the project.
- BDO noted that the Council's Whole of Government Accounts (WGA) submission is below the threshold for further work other than to submit the WGS Assurance Statement. This was submitted on 7 October 2016 ahead of national deadline.
- BDO reported that the review of grant claims and returns for 2015/16 is in progress, and the results will be reported on completion.
- BDO reviewed the governance arrangements for Council's New Homes Project, and made a number of recommendations for improvement that should be applied to future projects.

15.3 Grant Claims and Returns Certification for year ended 31 March 2015 (April 2016). The report was presented to the June 2016 meeting of the Committee. The key points were:

- The audit identified a high level of errors within the cases tested, which required a significant amount of extra testing by BDO and the Council. No amendments were made to the final claim submitted to DWP.
- The main errors were in the administration of benefits involving non-HRA rent rebates and rent allowances. There were a small number of cases of incorrect classification of expenditure as non-HRA, when the expenditure should have been classified as HRA rent rebates.
- The audit identified deficiencies in the Council's systems and controls around the identification of prior year uncashed payments, resulting in an under claim of £556.
- As a result of the errors found in administering benefits, BDO qualified the claim across all benefit expenditure types. The additional work required to be completed by the Council and BDO meant that the audited claim was submitted to DWP in March 2016, four months after the deadline date.
- The certification of the returns for the Pooling of Housing Capital Receipts was completed satisfactorily without amendment of certification. The main reported issue was the need for the Council to have in place appropriate plans to use retained receipts by certain milestone dates, otherwise the receipts must be paid to DCLG.

15.4 As was reported to the June 2016 meeting of the Committee, DWP made a marginal adjustment to the submitted claim which was agreed at a total value of approximately £35.8m.

16 Financial Appraisal

16.1 There are no additional financial implications from this report.

17 Sustainability Implications

17.1 I have not completed the Sustainability Implications Questionnaire as this report is exempt from the requirement because it is an internal monitoring report.

18 Risk Management Implications

18.1 If the Audit and Standards Committee does not ensure proper oversight of the adequacy and effectiveness of the Council's systems of internal control there is a risk that key aspects of the Council's control arrangements may not comply with best practice.

19 Legal Implications

19.1 There are no legal implications arising from this report.

20 Equality Screening

20.1 This report is for information only and involves no key decisions. Therefore, screening for equality impacts is not required.

21 Background Papers

21.1 Annual Audit Plan 2016/17

22 Appendices

22.1 Appendix A1: Statement of Internal Audit work and key issues.

22.2 Appendix A2: Table of abbreviations.

22.3 There is no Log of Significant Outstanding Recommendations (normally Appendix B) for this report.

APPENDIX A1

Statement of Internal Audit work and key issues

Audit Report: Newhaven Enterprise Centre (NEC)

Date of final issue: 7 December 2016

Overall opinion:
From the audit work carried out Internal Audit has obtained substantial assurance that there is a sound system of internal control covering the NEC. On the whole, compliance with controls is satisfactory, although there are a small number of issues that indicate there is scope to strengthen the way some controls are operated. The report contains two recommendations.

Main points:
Council carries out regular monitoring of the operation of the NEC, with regular site meetings with Basepoint representatives and examination of the quarterly Occupancy and Health and Safety reports provided by Basepoint. These monitoring arrangements mean that it is unlikely that any significant operational, safety or security issues would be overlooked but not all aspects of the contract are formally reviewed.

The NEC appears secure with CCTV monitoring of entrances and exits. Equipment and furniture assets are recorded and monitored by Basepoint, and are properly safeguarded. However, updates to the asset records are not forwarded to the LDC Insurance Officer, and no inventory audit has taken place since 2012. These points were both rectified during the audit.

Reasonable financial procedures are in place, which enable Council officers to account for income and expenditure, and to monitor the financial arrangements operated by Basepoint on the Council's behalf. The annual sampling of supporting documents for transactions completed at the NEC provides assurance as to the effectiveness of the financial procedures. These sampling checks were not completed in 2015/16 following changes in officer responsibilities, but the checks will take place in future.

Audit Report: Cemeteries

Date of final issue: 16 December 2016

Overall opinion:
From the audit work carried out during this review Internal Audit has obtained partial assurance that there is a sound system of internal control covering Cemeteries. Controls are in place and to an extent there is reasonable compliance. However, there are gaps in the control processes which weaken the system, and there is a need to introduce additional controls, or improve compliance with existing controls, to reduce the risk to the Council.

Main points:
Risks in cemeteries are being monitored but it appears some issues are not being identified and addressed. The weekly inspection sheets used by the contractor are not being completed properly in that it is not easy to determine the areas checked, no actions are noted and risk levels are not shown or are given as low risk. Site visits during the audit

noted collapsed/settled graves and cracked pathways. An external inspection of memorials was made and reported in 2015 but no action plan has been put in place to deal with the risks identified.

Burial capacity is a national long term issue, and there is an impending issue with burial capacity at Lewes. There are burial plots at Seaford to last for 10-15 years but there are only enough plots left in Lewes to provide two years' capacity. A report on this issue that was planned to go to Cabinet in November 2015 was not presented, and there has not been any further report prepared. A range of options for increasing capacity at Lewes are currently being considered.

The staff guidance notes covering the cemeteries service are not sufficiently detailed to enable any other officer to carry out the work adequately in the absence of those who have a full understanding of the procedures.

Audit Report: Insurance

Date of final issue: 20 December 2016

Overall opinion:
From the audit work carried out Internal Audit has obtained full assurance that there is a sound system of internal control covering insurance, and compliance with controls is good. In particular, insurable risks have been identified and assessed as the basis for arranging appropriate insurance cover. Procedures are in place to review and submit claims in reasonable time, and claims are monitored to ensure settlement within reasonable time. Levels and types of claims are monitored to identify possible areas for action to reduce risk and limit increases in insurance costs.

Main points:
Normally, audit reporting is by exception in that the findings and conclusions cover those areas that require attention, and recommendations outline the necessary changes in procedures and controls. The satisfactory situation means that there are no improvements that need to be made within the scope and objectives of the audit. The report contains no recommendations.

Appendix A2

Table of abbreviations

AGS – Annual Governance Statement
BCP – Business Continuity Planning
BDO – BDO, the Council's external auditors. Formerly BDO Stoy Hayward
CIPFA – Chartered institute of Public Finance and Accounting
CMT – Corporate Management Team
CTRS – Council Tax Reduction Scheme
DCLG – Department for Communities and Local Government
DFGs – Disabled Facilities Grants
DWP – Department of Work and Pensions
EBC – Eastbourne Borough Council
ESFOG – East Sussex Fraud Officers Group
HAFP – Head of Audit, Fraud and Procurement
HB – Housing Benefit
HRA – Housing Revenue Account. Refers to Council owned housing
ISO – International Organisation for Standardisation
IT – Information Technology
JTP – Joint Transformation Project
LDC – Lewes District Council
NFI – National Fraud Initiative
PIs – Performance Indicators
PSIAS – Public Sector Internal Audit Standards
QAIP – Quality Assurance and Improvement Programme
RTB – Right to Buy
SFIS – Single Fraud Investigation Service
WGA – Whole of Government Accounts

Agenda Item No:	**7**	**Report No:**	**14/17**
Report Title:	**Oversight of the Council's Surveillance Policy**		
Report To:	**Audit & Standards Committee**	**Date: 16 January 2017**	
Cabinet Member:	**Councillor Andy Smith**		
Ward(s) Affected:	**All**		
Report By:	**Catherine Knight, Assistant Director of Legal & Democratic Services**		

Contact Officer(s)-
Name(s): **Oliver Dixon**
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Purpose of Report:

To inform Audit & Standards Committee of its role in overseeing the Council's policy on the use of surveillance and related powers conferred by the Regulation of Investigatory Powers Act 2000.

Officers Recommendation(s):

1 To note the Council's updated policy on the use of powers under Part 2 of the Regulation of Investigatory Powers Act 2000, set out at Appendix 1

2 To note the role of Audit & Standards Committee in overseeing this policy.

Reasons for Recommendations

1 Cabinet has recently agreed an updated policy on the Council's use of powers under Part 2 of the Regulation of Investigatory Powers Act 2000. Responsibility for overseeing this policy and its proper implementation now lies with Audit & Standards Committee. It is therefore important for the Committee to be aware of the policy and understand their role in connection with it.

Information

2

2.1 On 4 January 2017, Cabinet agreed the updated policy, reproduced in full at Appendix 1, on the Council's use of statutory powers to conduct covert surveillance and deploy undercover operatives (known formally as 'covert human intelligence sources' – CHIS for short).

2.2 An update was necessary to reflect changes to the legislation from which the Council's covert surveillance and certain other intelligence-based powers are derived, namely Part 2 of the Regulation of Investigatory Powers Act 2000 ('RIPA') and associated secondary legislation.

2.3 The following legislative amendments are given effect in the updated policy:

(i) only Council officers of specified seniority may authorise the use of covert surveillance or the deployment of CHIS; and

(ii) following authorisation by a designated Council officer, proposed covert surveillance or use of a CHIS must be approved by a magistrate before either of those activities may commence.

2.4 The new policy also reflects Home Office guidance on the circumstances in which intelligence gathering via social media sites may amount to "directed surveillance" and which may therefore require prior authorisation in accordance with RIPA.

2.5 Cabinet considered that Audit & Standards Committee was the appropriate body to oversee the Council's implementation of, and adherence to, the updated policy. This is reflected in paragraph 12 of the policy (see Appendix 1). See also 2.10 (ii) below.

2.6 The Council makes little, if any, use of RIPA powers. Since 2008 it has not authorised any covert surveillance or CHIS. The policy makes clear that due to the strict controls imposed by the legislation and codes of practice, it is envisaged that the Council would make use of its powers under RIPA in exceptional circumstances only. Authorisation must be proportionate and a measure of last resort, where all other investigative options were deemed insufficient. This approach is reflected at paragraph 8 of the policy.

2.7 Despite the Council making no use of RIPA powers in recent years, the Office of Surveillance Commissioners (the national body responsible for overseeing the use of covert surveillance by designated public bodies) expects local authorities to maintain a state of readiness in case a situation arises when covert surveillance is necessary and proportionate. To this end, the Council is investing in refresher training for authorising officers and an on-line toolkit of procedures and processes.

2.8 It should be noted that the Council has power under Part 1 of RIPA, and only if strict conditions are met, to acquire communications data. This would include time, location and device details, but <u>not</u> the content. This power will in future be provided for under Part 3 of the Investigatory Powers Act 2016, when that Part comes into force, and will be broadly equivalent in scope. A minor difference is that Parliament has taken the opportunity under the 2016 Act to redefine the classes of communications data, to reflect current technology.

2.9 The Council has never needed to exercise its communications data acquisition powers, and it is not envisaged that it will become necessary to do so in the foreseeable future. In the unlikely event that use of these powers were necessary, their exercise would be subject to the same Member oversight as is proposed for the use of powers enabling covert surveillance and/or CHIS.

2.10 The updated policy includes two forms of internal checks on its operation:

(i) periodic internal audits, based on an assessment of risk, to ensure that officers are complying with statutory requirements and codes of practice;

(ii) Member oversight comprising officer reports to Audit & Standards Committee every 12 months on policy implementation, relevant legislative updates (if any), and the number of authorisations granted over the past year in exercise of RIPA powers.

Audit & Standards Committee are entitled to reports at more frequent intervals if they consider it necessary.

Thus, Members will have, through this Committee, an opportunity to raise concerns or queries over policy implementation, and to offer assurance to the Council and the local community that proper procedures and processes are being followed.

2.11 The Office of Surveillance Commissioners ('OSC') carry out a 3-yearly inspection of every local authority to check their arrangements for complying with RIPA. For authorities who have made little or no use of statutory powers since the previous inspection, OSC now begin with a paper exercise before deciding whether a personal visit is required. The Council's next OSC inspection is due in 2017/18.

Financial Appraisal

3 There are no financial implications arising from Audit & Standards Committee's proposed role regarding their oversight of surveillance arrangements.

Legal Implications

4 Oversight of the Council's use of RIPA powers are, following agreement by Cabinet on 4 January 2017, a proper function of Audit & Standards Committee.

The statutory framework governing covert surveillance and the conduct/use of CHIS is detailed in the body of the report.

The amendment referred to in paragraph 2.3(i) above derives from the Regulation of Investigatory Powers (Directed Surveillance and Covert Human Intelligence Sources) Order 2010; and the amendment referred to in paragraph 2.3(ii) derives from the Protection of Freedoms Act 2012. Both of these provisions resulted in amendments to Part 2 of RIPA.

Risk Management Implications

5 The Office of Surveillance Commissioners expects local authorities to put in place effective Member oversight of RIPA processes, so that officers who seek and authorise RIPA powers remain fully accountable. In the absence of Audit & Standard's oversight role, this level of accountability could be compromised.

Equality Screening

6 I have completed the initial Equality Impact Assessment screening exercise and no potential negative impacts were identified as a result of these recommendations; therefore a full Equality Impact Assessment is not required.

Background Papers

7 Report to Cabinet of 4 January 2017 on updated policy for use of powers under Part 2 of RIPA

Covert Surveillance and Property Interference Code of Practice (December 2014), issued by the Home Office

Covert Human Intelligence Sources Code of Practice (December 2014), issued by the Home Office

Procedures and Guidance: oversight arrangements for covert surveillance conducted by public authorities and to the activities of relevant sources (December 2014), issued by the Office of Surveillance Commissioners

Appendices

8 Appendix 1: Updated Policy on Use of Powers under Part 2 of RIPA

LEWES DISTRICT COUNCIL

POLICY STATEMENT ON USE OF POWERS UNDER REGULATION OF INVESTIGATORY POWERS ACT 2000, PART 2

Introduction

1. Lewes District Council ('the Council') is committed to building a fair and safe community for all by ensuring the effectiveness of laws designed to protect individuals, businesses, the environment and public resources.

2. The Council recognises that most organisations and individuals appreciate the importance of these laws and abide by them. The Council will use its best endeavours to help them meet their legal obligations without unnecessary expense and bureaucracy.

3. At the same time the Council has a legal responsibility to ensure that those who seek to flout the law are the subject of firm but fair enforcement action. Before taking such action, the Council may need to undertake covert surveillance of individuals and/or premises to gather evidence of illegal activity.

Procedure

4. All covert surveillance, whether physical or on-line, and any use of covert human intelligence sources ('CHIS'), shall be undertaken in accordance with the procedures set out in this document.

5. The Council shall ensure that covert surveillance and/or the use of CHIS is only undertaken where it complies fully with all applicable laws, in particular the:

   - Human Rights Act 1998
   - Regulation of Investigatory Powers Act 2000
   - Protection of Freedoms Act 2012
   - Data Protection Act 1998

6. The Council shall, in addition, have due regard to all official guidance and codes of practice, particularly those issued by the Home Office, the Office of Surveillance Commissioners (OSC), the Security Camera Commissioner and the Information Commissioner.

7. In particular, the following guiding principles shall form the basis of all covert surveillance and CHIS activity undertaken by the Council:

   (i) Covert surveillance and/or the use of CHIS shall only be undertaken where it is absolutely necessary in order to achieve the desired aims.

   (ii) Covert surveillance and/or the use of CHIS shall only be undertaken where it is proportionate to do so and in a manner that is proportionate.

   (iii) No monitoring of social network sites for investigation purposes shall take place without considering whether such monitoring constitutes directed surveillance; nor, where it is considered to be so, without obtaining the requisite prior authorisation and approval.

   (iv) Adequate regard shall be had to the rights and freedoms of those who are not the target of the covert surveillance.

(v) All authorisations to carry out covert surveillance and/or to use CHIS shall be granted by appropriately trained and designated authorising officers.

(vi) Covert surveillance regulated by RIPA and/or the use of CHIS shall only be undertaken after obtaining the approval of a magistrate.

8. With this mind, the Council has adopted a policy of not normally conducting covert surveillance and/or using CHIS but of doing so only as a last resort, where all other investigative options have been deemed insufficient. Whilst each situation will be considered on its own merits and all relevant factors will be taken into account, covert surveillance and/or the use of CHIS will be considered only where deemed a proportionate response of last resort.

Training and Review

9. All Council officers undertaking covert surveillance and/or using CHIS shall be appropriately trained to ensure that they understand their legal and moral obligations.

10. Regular audits shall be carried out to ensure that officers are complying with this policy.

11. The Senior Responsible Officer for RIPA (currently the Assistant Director of Legal and Democratic Services) shall review this policy at least once a year in the light of the latest legal developments and changes to official guidance and codes of practice.

12. The operation of this policy shall be overseen by Audit & Standards Committee by receiving reports every 12 months on this policy and its implementation, and on any RIPA activity conducted during the preceding 12-month period.

Conclusion

13. All citizens will reap the benefits of this policy, through effective enforcement of criminal and regulatory legislation and the protection that it provides.

14. Adherence to this policy will minimise intrusion into citizens' lives and will avoid any legal challenge to the Council's covert surveillance activities.

15. Any questions relating to this policy should be addressed to:

    Catherine Knight, Assistant Director of Legal & Democratic Services, RIPA Senior Responsible Officer

    Oliver Dixon, Lawyer and RIPA Co-ordinator

DATE: January 2017.

Agenda Item No: **8** **Report No:** **15/17**

Report Title: **Treasury Management**

Report To: **Audit and Standards Committee** **Date: 16 January 2017**

Ward(s) Affected: **All**

Report By: **Alan Osborne, Deputy Chief Executive**

Contact Officer(s)-

Name(s): **Stephen Jump**
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Purpose of Report:

To present details of recent Treasury Management activity

Officers Recommendation:

1. To confirm to Cabinet that Treasury Management activity between 1 November and 31 December 2016 has been in accordance with the approved Treasury Strategy for that period.

Reasons for Recommendations

1 Treasury Management Activity

1.1 The Council's approved Treasury Strategy Statement requires the Audit and Standards Committee to review details of Treasury Strategy transactions against the criteria set out in the Strategy and make observations to Cabinet as appropriate.

1.2 The timetable for reporting Treasury Management activity in 2016/2017 is shown in the table below. This takes into account the timescale for the publication of each Committee agenda and is on the basis that it is preferable to report on activity for complete months. Any extraordinary activity taking place between the close of the reporting period and the date of the Audit and Standards Committee meeting will be reported verbally at that meeting.

Meeting date	Reporting period for transactions
16 January 2017	1 November to 31 December 2016
20 March 2017	1 January to 28 February 2017

1.3 Fixed Term Deposits pending maturity

The following table shows the fixed term deposits held at 31 December 2016 and identifies the long-term credit rating of each counterparty at the date of investment. It is important to note that credit ratings are only one of the criteria that are taken into account when determining whether a potential counterparty is suitable. All of the deposits met the necessary criteria.

Ref	Counterparty	Date From	Date To	Days	Principal £	Int Rate %	Long-term rating
230916	Nationwide Building Society	18/08/16	20/02/17	186	1,000,000	0.40	A
231316	Thurrock Borough Council	05/10/16	04/01/17	91	1,750,000	0.25	*
231716	Thurrock Borough Council	21/10/16	23/01/17	94	500,000	0.25	*
232016	Thurrock Borough Council	28/11/16	30/05/17	183	3,000,000	0.35	*
233516	Nationwide Building Society	13/12/16	13/06/17	182	1,000,000	0.42	A
233616	Coventry Building Society	15/12/16	16/01/17	32	2,000,000	0.22	A
					9,250,000		

*UK Government body and therefore not subject to credit rating

1.4 Fixed Term Deposits which have matured in the reporting period

The table below shows the fixed term deposits which have matured since 1 November 2016, in maturity date order. It is important to note that the table includes sums reinvested and that in total the Council's investments have not increased by £38m over this period.

Ref	Counterparty	Date From	Date To	Days	Principal £	Int Rate %	Long-term rating
228716	Thurrock Borough Council	27/05/16	28/11/16	185	3,000,000	0.50	*
229716	Nationwide Building Society	06/06/16	06/12/16	183	1,000,000	0.71	A
232116	Coventry Building Society	01/11/16	15/11/16	14	2,000,000	0.20	A
232216	Debt Management Office	01/11/16	07/11/16	6	2,000,000	0.15	*
232316	Debt Management Office	02/11/16	07/11/16	5	1,000,000	0.15	*
232416	Debt Management Office	07/11/16	14/11/16	7	3,500,000	0.15	*
232516	Debt Management Office	08/11/16	14/11/16	6	2,000,000	0.15	*
232616	Debt Management Office	14/11/16	21/11/16	7	4,000,000	0.15	*
232716	Debt Management Office	15/11/16	24/11/16	9	1,500,000	0.15	*
232816	Coventry Building Society	15/11/16	22/11/16	7	2,000,000	0.19	A
232916	Debt Management Office	21/11/16	24/11/16	3	3,000,000	0.15	*
233016	Debt Management Office	22/11/16	24/11/16	2	1,000,000	0.15	*
233116	Debt Management Office	01/12/16	09/12/16	8	3,000,000	0.15	*
233216	Coventry Building Society	01/12/16	15/12/16	14	2,000,000	0.20	A
233316	Debt Management Office	06/12/16	13/12/16	7	1,000,000	0.15	*
233416	Debt Management Office	09/12/16	16/12/16	7	3,000,000	0.15	*
233716	Debt Management Office	15/12/16	19/12/16	4	1,000000	0.15	*
233816	Debt Management Office	15/15/16	22/12/16	7	2,000,000	0.15	*
	Total				38,000,000		

*UK Government body and therefore not subject to credit rating

At no stage did the total amount held by any counterparty exceed the approved limit set out in the Investment Strategy. The average rate of interest earned on deposits held in the period 1 November and 31 December 2016 was 0.44%, above the average bank base rate for the period of 0.25%. Those made during the period averaged 0.33%.

1.5 Use of Deposit accounts

In addition to the fixed term deposits, the Council has made use of the following interest bearing accounts in the period covered by this report, with the average amount held being £1.373m generating interest of approximately £400.

	Balance at 31 Dec '16 £'000	Average balance £'000	Current interest rate %
Santander Business Reserve Account	Nil	237	0.05%
Lloyds Bank Corporate Account	888	1,135	0.15%

1.6 Use of Money Market Funds

Details of the amounts held in the two Money Market Fund (MMF) accounts used by the Council are shown overleaf. The approved Investment Strategy allows a maximum investment of £3m in each fund, and at no time was this limit exceeded.

	Balance at 31 Dec '16 £'000	Average balance £'000	Average return %
Goldman Sachs Sterling Liquid Reserves Fund	3,000	2,873	0.39%
Deutsche Managed Sterling Fund	3,000	3,000	0.39%

1.7 Purchase of Treasury Bills (T-Bills)

The table below shows the T-Bills held at 31 December 2016 and activity in the period. It is the Council's intention to hold T-Bills until maturity.

	Maturity Date .	Purchased in period	Purchase date	£'000	Disc %
Held at 31 December 2016					
UK Treasury Bill 0%	03 Jan 17		04 Jul 16	1,000	0.420

The average discount (ie the gross return) achieved on T-Bills held in the period was 0.42%. No T-Bills matured, or were purchased, during the period.

1.8 Secured Investments

The investments overleaf are secured against the assets of the bank. The interest rate can vary, by reference to changes in the 3 month 'London Interbank Offered Rate (LIBOR)'.

Ref	Counterparty	Date From	Date To	Days	Principal £	Current Rate %	Long Term Rating
XS0769914218	Abbey National Treasury	12 May 16	05 Apr 17	328	1,000,000	0.681	AAA
XS113251472	Bank of Nova Scotia	22 Jul 16	02 Nov 17	414	2,000,000	0.567	AAA
					3,000,000		

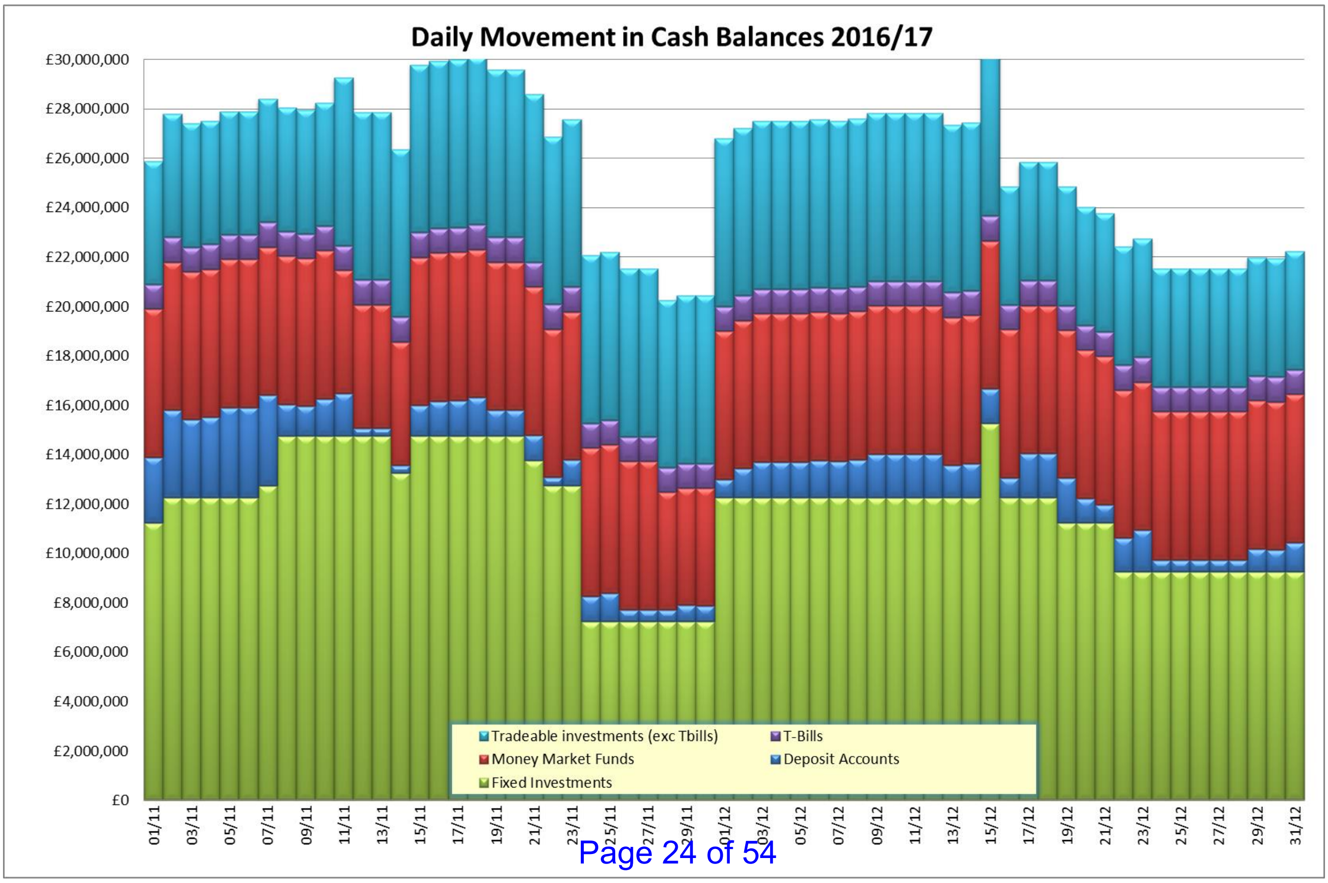
1.9 Tradeable Investments

The table below shows the Tradeable Investments held at 31 December 2016 and activity in the period. It is the Council's intention to hold investments until maturity.

Ref	Counterparty		Date From	Date To	Days	Principal £	Rate %	Long Term Rating
Held at 31 December 2016 (purchased in period)								
XS0966280561	Svenska Handelsbanken	FB	11 Nov 16	29 Aug 17	291	618,000	0.616	AAA
XS0434423926	Unilever Plc	FB	11 Nov 16	16 Jun 17	217	1,110,000	0.475	AAA
						1,728,000		
Matured in period								
32264	Rabobank	CD	16 Aug 16	16 Dec 16	122	2,000,000	0.360	AAA
FB – Fixed Bond	CD – Certificate of Deposit							

1.10 Overall investment position

The chart below summarises the Council's investment position over the period 1 November to 31 December 2016. It shows the total sums invested each day as Fixed Term deposits, T-Bills, amounts held in Deposit accounts, MMFs and Tradeable Investments.



1.11 Borrowing

No temporary borrowing has been undertaken and the current account with Lloyds Bank remained in credit throughout the period.

There has been no change in the total value of the Council's long term borrowing in the reporting period, which remains at £56.673m.

Financial Implications

2 All relevant implications are referred to in the above paragraphs.

Risk Management Implications

3 The risk management implications associated with this activity are explained in the approved Treasury Management Strategy. No additional implications have arisen during the period covered by this report.

Equality Screening

4 This is a routine report for which detailed Equality Analysis is not required to be undertaken.

Legal Implications

5 None arising from this report.

Background Papers

Treasury Strategy Statement http://www.lewes.gov.uk/council/20987.asp

Agenda Item No:	**9**	**Report No:**	**16/17**
Report Title:	**Annual Treasury Management Strategy Statement and Investment Strategy 2017/2018 to 2019/2020**		
Report To:	**Audit and Standards Committee**	**Date: 16 January 2017**	
Ward(s) Affected:	**All**		
Report By:	**Alan Osborne, Deputy Chief Executive**		

Contact Officer(s)-

Name(s): **Stephen Jump**
Post Title(s): **Head of Finance**
E-mail(s): **steve.jump@lewes.gov.uk**
Tel No(s): **01273 471600**

Purpose of Report:

To present the draft Treasury Management Strategy Statement and Investment Strategy 2017/2018 to 2019/2020.

Officers Recommendation:

1. To receive the draft Treasury Management Statement and Investment Strategy 2017/2018 to 2019/2020 and make comments to Cabinet as the Committee sees fit.

2. To note the contents of this report.

Reasons for Recommendations

1 The Council has adopted the CIPFA Code of Practice on Treasury Management. In accordance with the Code of Practice, the Cabinet approves an updated Annual Treasury Strategy Statement before the start of each financial year. This includes an Investment Strategy for the year ahead (which Government guidance notes should be adopted by full Council) as well as 'Prudential Indicators' which are required to be set in order to comply with the 'Prudential Code for Capital Finance in Local Authorities' (The Prudential Code).

2 It is appropriate for the Audit and Standards Committee to review and comment on the draft Strategy before it is approved by Cabinet as part of the overall budget cycle, rather than to carry out this function after the Strategy has been formally adopted.

Information

1 Purpose of the Strategy Statement

1.1 The draft Strategy Statement is attached at Appendix 1. It sets out the background to the Council's treasury management activity both in terms of the wider economy and the Council's own current and projected financial position. It sets out the approach which will be taken to borrowing and the investment of cash balances. It explains the risks which are inherent in treasury management and how these are to be mitigated. The Strategy Statement specifies the Prudential Indicators which the Council is to set in order to meet the requirements of the Prudential Code; contains an 'MRP Statement' which defines the approach that the Council will take to make prudent provision for debt redemption; and establishes the policy for the separate management of General Fund and Housing Revenue Account borrowing.

1.2 The content of the draft Strategy Statement follows the requirements of CIPFA's revised Code of Practice which was published in November 2011 and has been prepared with the support of Arlingclose, the Council's Treasury advisers.

1.3 It is important to note that values shown in the draft Strategy Statement (eg capital expenditure, use of reserves, capital financing requirement) are best estimates at the time of preparing the report, and may be revised when draft budget papers are finalised for consideration by Cabinet at its February meeting. Any revisions are expected to be immaterial, with no bearing on the Strategy proposed.

1.4 In 2016/2017 the Council has expanded its commercial property portfolio to generate revenue income streams. This investment of financial resources in property assets, is outside the remit of (though has an impact on) this Strategy which has a remit of treasury management activity only.

2 2017/2018 Strategy Statement in context

2.1 Given the risk and continued low returns from short-term unsecured bank investments, the Strategy enables the Council to continue diversification into more secure and/or higher yielding asset classes during 2017/2018. Diversification is of importance in the context of the Council's reserves and balances reducing as they are called on to support the Council's organisational change programme. With diminishing reserves, the impact of a single counterparty default would be greater.

3 Proposed Changes to Investment Strategy

3.1 The minimum credit rating for investments permissible under the current Strategy is long-term 'A-'. This was more cautious than Arlingclose's recommended minimum of long-term 'BBB+' for 2016/2017.

3.2 Arlingclose continue to advise a minimum credit rating criteria of long-term 'BBB+, one mark below the 'A-' rating and it is proposed to move to that level for 2017/2018, increasing investment opportunities.

3.3 The current Strategy limits the total of long-term investments (ie more than one year) to £2m. Arlingclose advise that clients should seek longer term-investment opportunities, where funds are known to be available, which brings the potential for higher returns. It is proposed, therefore, to increase the limit for the total of long-term investments (ie more than one year) to £3m from the current limit of £2m.

3.4 The current strategy precludes investments with corporate institutions or registered providers (housing associations) with a credit rating of A-. Arlingclose advise that investment with such counterparties is appropriate, and it is proposed to amend the Strategy accordingly.

3.5 Appendix C (page 21) of the Strategy sets out approved counterparty types and limits for 2017/2018 in detail. A limit of £2m per counterparty will apply, with the exception of investments with Government bodies (unlimited) and pooled funds, for example Money Market Funds, for which the individual limit will be £3m. With the exception of the change to the credit rating criteria referred to above, all counterparty types and investment durations remain unchanged from the current Strategy.

3.6 It should be noted that the presence of a counterparty type on the list at Appendix C does not necessarily mean that it will be used by the Council.

4 Borrowing Strategy

4.1 The current approach of 'internal borrowing' (ie using cash held as balances, reserves and working capital as an alternative to long-term borrowing) as a means of funding capital expenditure will continue in 2017/2018.

4.2 The Council will remain open to the possibility of debt rescheduling (ie replacing an existing loan with a new loan or loans, or repaying a loan without replacement) where this is expected to lead to an overall saving or reduction in risk.

5 Provision for debt repayment

5.1 Local authorities are required to make prudent provision for the repayment of debt, and set its Policy for doing so each year. With the Council increasingly looking to extend its commercial property portfolio, develop its land holdings and realise assets, the Policy has been amended to identify how associated debt will be treated. This is set out in Section 13 of the Strategy.

6 Prudential Indicators

A number of the Prudential Indicators relate to elements of the Capital Programme and General Fund and Housing Revenue Account budgets which are to be considered by Cabinet in February 2017 as a full 'budget package'. It is not possible to include future values for these Prudential Indicators at this stage, and they are outside the scope of the Audit and Standards Committee's review. Appendix B to the Strategy document has, therefore, been excluded from these papers.

7 **Financial Implications** - All relevant implications are referred to in the Draft Strategy Statement.

8 **Legal Implications -** The legislative context is set out in the Draft Strategy Statement.

9 **Risk Management Implications -** The risk management implications associated with this activity are explained in the Draft Strategy Statement.

10 **Equality Screening -** The contents of this report is technical in nature, relating to the management of the Council's investments and borrowing. As such, Equality Screening was not required.

Appendix 1 – Draft Treasury Management Statement and Investment Strategy 2017/2018 to 2019/2020

Background Papers – Treasury Strategy Statement 2016/2017 http://www.lewes.gov.uk/council/20987.asp

Lewes District Council

Treasury Management Strategy Statement and Investment Strategy 2017/18 to 2019/2020

Contents

1. Executive Summary

1.1 Borrowing – the Council can borrow to finance capital expenditure in a similar way to an individual taking out a mortgage to buy a house. At 31 March 2017, total cumulative capital expenditure which will need to be funded amounts to £79.5 m. The actual long term-borrowing (the mortgage) that we have is only £56.7m because we are using the cash held in our reserves to make up the difference, rather than invest that money. (See Sections 6 and 7 for the details).

1.2 Debt rescheduling – The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk. (See Section 8 for the details).

1.3 Accounting for debt – the Council will adopt a two-Pool approach in order to manage and account for the debt of the General Fund/Housing Revenue Account. (See Section 9 for the details).

1.4 Investing – at any given time, the Council has varying amounts of cash consisting of reserves and balances, as well as working capital, which must be held securely. The security of our investments is our highest priority. We have defined the types of investment that we will make and the criteria that those organisations with which we will deal must meet. (See Sections 10 and 11 for the details).

1.5 Providing for the repayment of debt – we will continue to make annual provisions to repay our long term borrowing. (See Section 13 for the details).

1.6 Reporting – we will closely monitor our Treasury Management activity and make reports to every meeting of the Council's Audit and Standards Committee, with quarterly reports to Cabinet. (See Section 14 for the details).

2. Treasury Management Defined

2.1 The Council defines its Treasury Management activities as:

"the management of the Council'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."

2.2 Treasury Management is not undertaken in isolation. The Council acknowledges that effective Treasury Management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in Treasury Management and ensuring that performance is monitored and reported. All Treasury Management activity takes place within the context of effective risk management.

3. Scope of the Treasury Management Strategy Statement

3.1 This Strategy Statement sets out the Council's approach to financing (borrowing) and investment for the financial year but also sets the context for the following two years.

3.2 The Council has adopted the Chartered Institute of Public Finance and Accountancy's (CIPFA's) Code of Practice for Treasury Management in Public Services (the "TM Code"). This requires local authorities to determine the Treasury Management Strategy Statement (TMSS) before the start of the financial year.

3.3 The Department for Communities and Local Government. (DCLG) issued revised 'Guidance on local Authority Investments' in 2010 that requires each local authority to approve an investment strategy before the start of each financial year. This Strategy Statement incorporates that formal Investment Strategy.

3.4 The Strategy sets out the context to Treasury Management in terms of the Council's financial resources as measured in its Balance Sheet and external factors, in particular the outlook for interest rates. It considers how the Revenue Budget and Capital Programme will impact on the Balance Sheet position.

3.5 In accordance with the DCLG Guidance, the Council will be asked to approve a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change in interest rates, or in the Council's capital programme or in the level of its investment balance.

4. Approach to Risk

4.1 The Council has borrowed and expects to invest substantial sums of money and is therefore exposed to financial risks including the revenue effect of changing interest rates and, in the extreme, the loss of invested funds.

4.2 The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its Treasury Management activities will be measured. Accordingly, the analysis and reporting of Treasury Management activities will focus on their risk implications for the Council. No Treasury Management activity is without risk. The main risks to the Council's Treasury activities are:

- Credit and Counterparty Risk (security of investments)
- Liquidity Risk (adequacy of cash resources)
- Market or Interest Rate Risk (exposure to fluctuations in interest rate levels)
- Inflation Risk (exposure to inflation)
- Refinancing Risk (impact of debt maturing in future years)
- Legal & Regulatory Risk (compliance with statutory powers and regulatory requirements)

- Fraud, Error and Corruption and Contingency Management (maintenance of sound systems and procedures)

5. External Context

5.1 Economic Background

The major external influence on the Council's treasury management strategy for 2017/18 will be the UK's progress in negotiating a smooth exit from the European Union. Financial markets, wrong-footed by the referendum outcome, have been weighed down by uncertainty over whether leaving the Union also means leaving the single market. Negotiations are expected to start once the UK formally triggers exit in early 2017 and last for at least two years. Uncertainty over future economic prospects will therefore remain throughout 2017/18.

The fall and continuing weakness in sterling and the near doubling in the price of oil in 2016 have combined to drive inflation expectations higher. The Bank of England is forecasting that Consumer Price Inflation will breach its 2% target in 2017, the first time since late 2013, but the Bank is expected to look through inflation overshoots over the course of 2017 when setting interest rates so as to avoid derailing the economy.

Initial post-referendum economic data showed that the feared collapse in business and consumer confidence had not immediately led to lower GDP growth. However, the prospect of a leaving the single market has dented business confidence and resulted in a delay in new business investment and, unless counteracted by higher public spending or retail sales, will weaken economic growth in 2017/18.

Looking overseas, as expected the US Federal Reserve increased the target range for official interest rates for just the second time in the last decade. The range was increased to between 0.5% and 0.75%, from 0.25% and 0.5%. The accompanying statement by Fed Chair, Janet Yellen, suggested that they currently expect three rate hikes in 2017 and in both 2018 and 2019. What is much less predictable are the actual economic consequences of the economic policies that will accompany the incoming Trump presidency. The markets, including the Federal Reserve, are presumably confident that the outcome is likely to result in higher inflation and the need for higher interest rates.

The Eurozone meanwhile has continued to struggle with very low inflation and lack of momentum in growth.The impact of political risk on financial markets remains significant over the next year. With challenges such as immigration, the rise of populist, anti-establishment parties and negative interest rates resulting in savers being paid nothing for their frugal efforts or even penalised for them, the outcomes of the French presidential and general elections (April – June 2017) and the German federal elections (August – October 2017) have the potential for upsets.

5.2 Credit Outlook

Markets have expressed concern over the financial viability of a number of European banks recently. Sluggish economies and continuing fines for pre-crisis behaviour have weighed on bank profits, and any future slowdown will exacerbate concerns in this regard.

Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the European Union, Switzerland and USA, while Australia and Canada are progressing with their own plans. The credit risk associated with making unsecured bank deposits has therefore increased relative to the risk of other investment options available to the Council; returns from cash deposits however continue to fall.

5.3 Outlook for Interest Rates

The detailed economic interest rate outlook provided by the Council's Treasury advisor, Arlingclose Ltd, is attached at Appendix A. The Arlingclose central case is for Bank Rate to remain at 0.25% through to March 2020, but there is a low possibility of a drop to close to zero. Negative Bank Rate is currently perceived by some policymakers to be counterproductive but, although a low probability, cannot be entirely ruled out in the medium term, particularly if the UK enters recession as a result of concerns over leaving the European Union.

Gilt yields have risen sharply, but remain at low levels. Arlingclose is projecting the 10 year gilt yield (which is an indicator of borrowing rates) to decline from 0.95% to 0.90% when the Government triggers Article 50.

5.4 Interest rates are of fundamental importance to the Council's Treasury Management operation. The ideal scenario would be to make short-duration investments if interest rates are low and are expected to rise significantly in the near future and to invest for longer periods if interest rates are considered to be close to their peak. In terms of borrowing, it is preferable to borrow short-term when interest rates are high and expected to fall and to undertake long-term borrowing when interest rates are low and expected to rise.

5.5 The estimate for external interest payments in 2017/2018 is £1.73m, unchanged from 2016/2017, which reflects the stability of the loan portfolio at fixed interest rates. The estimate for external interest receipts is £0.104m, unchanged from 2016/2017 in which year actual interest returns have exceeded the budget.

5.6 The Council's need to borrow and its ability to invest are interrelated, as explained elsewhere in this Strategy Statement. The Council will reappraise its strategy in both of these areas from time to time and, if needs be, realign it with evolving market conditions and expectations for future interest rates. Any such changes will require the prior approval of Cabinet.

6. The Need to Borrow Long Term

6.1 Other than for temporary cash flow purposes, local authorities are only allowed to borrow to finance capital expenditure (eg the purchase of property, vehicles or equipment which will last for more than one year, or the improvement of such assets). The Government limits the amount borrowed by local authorities for housing purposes only by specifying 'debt caps'. This Council's underlying debt cap has been fixed at £72.931m. In 2014/2015 local authorities were able to bid for an increase in its housing debt cap in order to enable specific projects. A bid from this Council was successful and this Council's debt cap will increase to a maximum of £75.248m to match expenditure incurred in building new houses on 7 specified former garage sites.

6.2 In accounting terms, the underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. In recent years, the Council's strategy has been to maintain borrowing and investments below their underlying levels, known as internal borrowing, and this remains the Strategy for 2017/2018.

6.3 The CFR is, in simple terms, the amount of capital expenditure which has been incurred by the Council but which has not yet been paid for (by using, for example, grants, capital receipts, reserves or revenue income) and in the meantime is covered by internal or external borrowing. 'External borrowing' is where loans are raised from the Public Works Loans Board (PWLB) or banks. Alternatively it is possible to 'internally borrow' the significant levels of cash which has been set aside in Balances and Reserves and which would otherwise need to be invested with banks or other counterparties..

6.4 The CFR is calculated each year in accordance with a statutory formula. As noted above, the level of CFR increases each year by the amount of capital expenditure which is yet to be financed and is reduced by the amount that the Council sets aside for the repayment of borrowing. This is illustrated in the table below. Amounts from 2017/2018 onwards are indicative. Projected capital expenditure in 2017/2018 with a financing requirement comprises allocations for new housing (£0.3m) and commercial development projects (£4.9m) which will generate rental income to support the General Fund budget.

	2015/16 £m	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
Opening CFR	69.979	71.531	79.531	83.785	86.875
Capital exp in year	12.957	23.953	14.112	10.536	9.076
Less financed	(9.378)	(12.767)	(8.722)	(6.303)	(4.891)
Less amount set aside for debt repayment	(2.027)	(3.186)	(1.136)	(1.143)	(1.350)
Closing CFR	**71.531**	**79.531**	**83.785**	**86.875**	**89.710**

6.5 The overall CFR can be split between the General Fund and Housing Revenue Account as follows:

	2015/16 £m	2016/17 £m	2017/18 £m	2018/19 £m	2019/20 £m
General Fund	7.607	13.849	18.656	22.401	25.895
HRA	63.924	65.682	65.129	64.474	63.815
Total CFR	**71.531**	**79.531**	**83.785**	**86.875**	**89.710**

6.6 The following table compares the CFR with the amount that the Council holds in balances and reserves as well as working capital (day to day cash movements as well as grants, developer contributions and capital receipts held pending use):

	31/3/16 £m	31/3/17 £m	31/3/18 £m	31/3/19 £m	31/3/20 £m
(a) Capital Financing Requirement	71.531	79.531	83.785	86.875	89.710
(b) Actual external borrowing	(56.673)	(56.673)	(56.673)	(56.673)	(56.673)
(c) Use of Balances, Reserves and working capital as alternative to borrowing (a)–(b)	14.858	22.858	27.112	30.202	33.037
(d) Total Balances and Reserves	17.343	13.637	12.532	12.443	13.766
(e) Working capital	15.909	15.034	17.170	20.313	21.663
(f) Amount used as an alternative to borrowing (c) above	(14.858)	(22.858)	(27.112)	(30.202)	(33.037)
(g) Total investments (d)+(e)+(f)	18.394	5.813	2.590	2.554	2.392

6.7 The table above (line b) assumes that the current external loan portfolio is unchanged across the period. The potential for and approach to repaying or rescheduling existing loans is explained in Section 8 below.

6.8 Line g in the table above indicates that it will be possible to continue the current approach of internal borrowing as an alternative to raising new external loans, which remain at their current level across the period (line b). However, it will be necessary to monitor the position closely as projections of the capital programme, use of reserves, capital receipts generated from the sale of assets and the level of working capital shown in the later years are less certain. Market conditions, interest rate expectations and counterparty and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying Balance Sheet position. The following section explains the approach to borrowing in more depth.

7. Borrowing Strategy

7.1 As noted above, the Council's underlying need to borrow for capital purposes is measured by reference to its CFR. In respect of General Fund activities, local authorities are required to make a charge to Revenue budgets each year at a prudent level, ensuring that the underlying need to borrow is eliminated over the longer term period across which the initial expenditure continues to provide economic benefit.. This charge is known as the Minimum Revenue Provision for Debt Redemption (MRP). There is no requirement to make a provision to reduce HRA borrowing, although it is prudent to do so.

7.2 Capital expenditure not paid for from internal resources (i.e. Capital Receipts, Capital Grants and Contributions, Revenue or Reserves) will produce an increase in the CFR (the underlying need to borrow) and in turn produce increased annual MRP charges in the Revenue Account.

7.3 In accordance with the Prudential Code, the Council will ensure that net external borrowing does not, except in the short term, exceed its highest CFR over the next three years.

The cumulative estimate of the Council's long-term borrowing requirement in respect of historic and planned capital expenditure is shown in the table below. As explained in paragraph 6.4, the increases in the CFR are largely the result of investment in commercial property which will generate annual rental income streams.

	31/03/2017 Estimate £m	31/03/2018 Estimate £m	31/03/2019 Estimate £m	31/03/2020 Estimate £m
Capital Financing Requirement	79.5	83.8	86.9	89.7
Less: Profile of current Borrowing	(56.7)	(56.7)	(56.7)	(56.7)
Cumulative Maximum External Borrowing Requirement	22.8	27.1	30.2	33.0

7.4 The Council's chief objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required. The flexibility to renegotiate loans should the Council's long-term plans change is a secondary objective.

7.5 Given the projected reduction in revenue funding from the Government through to 2019/2020 and the Council's General Fund savings target of £2.7m over that period, the Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio, With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead. By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. For example, the current rates (January 2017) available to the Council for 2-year and 5-year PWLB maturity loans are 1.17% and 1.64% respectively compared with 0.15% which can be earned on a temporary deposit with the Government.

7.6 The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. At some stage the level of General Fund Reserves and Balances will become depleted (as they are used for the purpose for which the funds were set aside) restricting the ability to borrow internally.

7.7 The Council's appointed Treasury advisor, Arlingclose, will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2017/2018 with a view to keeping future interest costs low, even if this causes additional cost in the short-term. Alternatively, the Authority may arrange forward starting loans during 2017/2018, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period Any decision to borrow will be confirmed with the Cabinet Member for Finance and reported to the next meeting of the Cabinet.

7.8 The Council may borrow short-term loans (normally up to one month) to cover unexpected cash flow shortages should they arise.

7.9 The approved sources of new long-term and short-term borrowing will be:

- Public Works Loans Board (and any successor body)
- UK Local Authorities
- any institution approved for investments (see Section 11) below
- UK public and private sector pension funds (except East Sussex County Council Pension Fund)
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

In the event that alternative sources of borrowing are identified in the year, which are considered to be more appropriate in the context of the overall strategy, a report will be made to Cabinet and Council. Arlingclose will assist the Council with the analysis of options.

7.10 The Council has previously raised the majority of its long-term borrowing from the PWLB but it will investigate other sources of finance, such as local authority loans and bank loans, which may be available at more favourable rates.

7.11 The Local Government Association established the UK Municipal Bonds Agency plc in 2014 as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for a number of reasons including the fact that there will be a lead time of several months between committing to borrow and knowing the interest rate payable. Any decision to borrow from this source will therefore be the subject of a separate report to full Council.

8. Debt Rescheduling

8.1 At the time of preparing this Strategy, the Council's loan portfolio was as shown in the table overleaf. All of the PWLB loans listed below were taken out in March 2012 in order to finance the payment to the Government needed for the national transition to self-financing for local authority housing. The Barclays loan shown in the table above was taken out in April 2004 with a term of 50 years maturing in April 2054. The bank has now decided to permanently waive its initial contractual right to change the interest rate on this loan, which effectively becomes fixed at the current rate of interest 4.5%.

Lender	Interest	Amount £m	Rate %	Maturity
PWLB	Fixed	4.00	2.7000	01/03/2024
PWLB	Fixed	5.00	3.3000	01/03/2032
PWLB	Fixed	2.00	3.0500	01/09/2027
PWLB	Fixed	2.00	2.7600	01/09/2024
PWLB	Fixed	4.00	2.9700	01/09/2026
PWLB	Fixed	5.00	3.2800	01/09/2031
PWLB	Fixed	4.00	2.6300	01/09/2023
PWLB	Fixed	5.00	3.4400	01/03/2037
PWLB	Fixed	6.67	3.5000	01/03/2042
PWLB	Fixed	5.00	3.4300	01/09/2036
PWLB	Variable	5.00	0.6200	28/03/2022
PWLB	Fixed	4.00	3.0100	01/03/2027
	Sub-total	51.67		
Barclays	Fixed	5.00	4.5000	06/04/2054
	Total	56.67		

8.2 The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to set a formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall saving or reduction in risk. Any intended debt rescheduling activity will be confirmed with the Cabinet Member for Finance and reported to the next Cabinet meeting.

9. The Housing Revenue Account Share of Treasury Management Costs.

9.1 Local authorities are required to recharge interest expenditure and income attributable to the HRA in accordance with Determinations issued by the DCLG. The Determinations do not set out a methodology for calculating the interest rate to use in each instance. The Council is therefore required to adopt a policy that will set out how interest charges attributable to the HRA will be determined. The CIPFA Code recommends that authorities present this policy in their Strategy Statement.

9.2 The Council has adopted a ‘2 pool’ (General Fund and HRA) approach to accounting for long-term loans. All current loans were allocated to the HRA on the introduction of ‘self-financing’. Any new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account.

9.3 At the start of each year, an assessment will be made of the difference between the value of the HRA loans pool and the HRA’s underlying need to borrow (adjusted for HRA balance sheet resources available for investment). If the resulting cash balance is negative, an ‘internal loan’ will be advanced from the General Fund (Reserves and Balance) to the HRA and interest charged at a rate equivalent to a one-year maturity loan from the PWLB at the start of the financial year. This is a reasonable approach and reflects the fact that strategic borrowing decisions will generally be made on an annual basis, as demonstrated in this Strategy. The same approach will be adopted for any new internal borrowing required in the year to support the cost of HRA capital expenditure not anticipated in the initial annual capital programme.

10. The Need to Invest

10.1 As shown in the table in paragraph 6.6 the Council currently holds healthy Reserves and Balances (£13.6m projected at 31 March 2017 excluding working capital eg s106 Developer Contributions and Capital Receipts which will be used to fund the future Capital Programme). In simple terms, Reserves represent amounts of money which have been set aside for use in future years for specific purposes (eg to pay for the replacement of vehicles at the end of their useful life) and Balances are cash which is retained both to ensure that the Council is able to respond effectively if an unforeseen event arises (eg the failure of a major contractor) and also to act as a buffer against unpredicted cash flow movements. Reserves and Balances are forecast to reduce over the next three years as they are called upon to support projects, services and the Council’s Joint Transformation Programme.

10.2 Although a proportion of the Reserves and Balances are being used as an alternative to external long-term borrowing, this still leaves a residual amount as retained cash. In addition, the Council’s cash flow movements fluctuate on a day to day basis, with cash received exceeding cash paid out at key points over the year. For example, at the start of 2016/2017 £13m was available for investment but the maximum amount invested at any point in the year was £30m. The purpose of the Investment Strategy is to define the conditions under which this ‘surplus’ cash is to be managed, with the priority being security of the sums invested.

10.3 DCLG Guidance on Local Government Investments in England requires authorities to set an Annual Investment Strategy. The speculative procedure of borrowing purely in order to invest is unlawful. However, taking on new external loans to reduce the level of internal borrowing is permissible, and, if this takes place, the Council will place importance on the flexibility of its loan portfolio as well as the liquidity of its investments.

11. Investment Strategy

11.1 The Council's general policy objective is to invest its surplus funds prudently, striking a balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Authority will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

11.2 The Council's investment priorities are:

highest priority -	security of the invested capital;
followed by -	liquidity of the invested capital (this enables the Council to react to changing circumstances)
finally -	an optimum yield which is commensurate with security and liquidity.

11.3 If the UK enters into a recession in 2017/2018, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

11.4 Given the increasing risk and falling returns from short-term unsecured bank investments, the Council aims to diversify into more secure and/or higher yielding asset classes during 2017/2018. This is especially the case for funds that are identified as being available for longer-term investment. This diversification will represent a continuation of the strategy adopted in 2015/2016 and implemented in 2016/2017.

11.5 The Council may invest its surplus funds with any of the counterparty types identified in Appendix C, subject to the cash limits (per counterparty) and the time limits shown. It is important to note that not all of the types of investment listed above will necessarily be used in 2017/2018, and some have not been used previously. Before any type of investment instrument is used for the first time, the advice of Arlingclose will be sought.

11.6 Investment limits are set by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used. However, investment decisions are never made solely based on credit ratings, and all other relevant factors including external advice will be taken into account.

11.7 The Council and its advisors remain vigilant at all times, monitoring signs of credit or market distress that might adversely affect the Council.

11.8 Credit ratings are obtained and monitored by Arlingclose who will notify changes in ratings as they occur. Where a counterparty has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made
- any existing investments that can be recalled or sold at no cost, will be
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty

11.9 Where a rating agency announces that a rating is on review for possible downgrade (also known as 'rating watch negative') below the approved investment criteria, then only investments that can be withdrawn on the next working day will be made with that counterparty until the outcome of the review is announced. This approach will not apply to 'negative outlooks' which indicate a long-term direction of travel rather than an imminent change of rating.

11.10 The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

11.11 When deteriorating financial market conditions affect the credit worthiness of all organisations (as happened in 2008 and 2011), this is not generally reflected in credit ratings, but can be seen in other market measures. In these circumstances the Council will restrict its investments to those organisations of higher credit quality and reduce the maximum duration of its investments to maintain the required level of security. The extent of these restrictions will be in line with prevailing financial market conditions. If these restrictions mean that insufficient commercial organisations of high credit quality are available for the investment of the Council's cash balances, then the surplus will be deposited with the UK Government, via the Debt Management Office or invested in government treasury bills for example, or with other local authorities. This will cause a reduction in the level of investment income earned, but will protect the principal sum invested.

11.12 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the DCLG Guidance.

Specified investments are

- denominated in £ sterling
- due to be repaid within 12 months of arrangement
- not defined as capital expenditure by legislation

- invested with the UK Government or local authority or a body or investment scheme of high credit quality'

11.13 The Council defines 'high credit quality' organisations and securities as those having a long-term credit rating of A- or higher that are domiciled either in the UK or in a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds 'high credit quality' is defined as those having a credit rating of A- or higher.

11.14 Any investment not meeting the definition of a specified investment is classed as non-specified. The Council does not intend to make any investments denominated in foreign currencies nor any that are defined as capital expenditure (eg company shares). Non-specified investments will therefore be limited to long-term investments ie those that are due to mature 12 months or longer from the date of arrangement and investments with bodies and schemes not meeting the definition of 'high credit quality'.

Limits on non-specified investments are shown below.

	Cash limit
Total long-term investments	£3m
Total investments rated below A-	£5m
Total investments (except pooled funds) with institutions domiciled in foreign countries rated below AA+	£2m
Total non-specified investments	£10m

11.15 The Council's revenue reserves available to cover investment losses are forecast to be £9m on 31st March 2017. The maximum that will be lent to any one organisation (other than the UK Government) will be £2m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below. Investments in pooled funds and multilateral development banks do not count against the limit for any single foreign country, since the risk is diversified over many countries.

	Cash limit
Any single organisation, except the UK Central Government	£2m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£2m per group
Any group of pooled funds under the same management	£3m per manager
Negotiable instruments held in a broker's nominee account	£10m per broker/account
Foreign countries	£3m per country
Registered Providers	£4m in total
Money Market Funds	£10m in total

11.16 The Deputy Chief Executive will undertake the most appropriate form of investments in keeping with the investment objectives, income and risk management requirements and Prudential Indicators. Confirmation that investments have been made in accordance with the Strategy will be reported to meetings of the Audit and Standards Committee and Cabinet. Investment returns will be benchmarked quarterly against the average published 7 day LIBID rate.

11.17 All of the Council's investments are currently managed in-house and this approach will continue for the duration of this Strategy unless otherwise approved in advance by Cabinet.

11.18 The Council uses a spreadsheet model, updated daily, to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

11.19 Investment of Money Borrowed in Advance of Need: The Council may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council's overall management of its treasury risks. The maximum period between borrowing and expenditure is expected to be two years, although the Council is not required to link particular loans with particular items of expenditure.

12. The Use of Financial Instruments for the Management of Risks

12.1 Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (eg interest rate collars and forward deals) and to reduce costs or increase income at the expense of greater risk (e.g. LOBO loans and callable deposits). The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over local authorities' use of standalone financial derivatives (ie those that are not embedded into a loan or investment).

12.2 The CIPFA Code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy. The Council will only use standalone financial derivatives (such as swaps, forwards, futures and options) where they can be clearly demonstrated to reduce the overall level of the financial risks that the Council is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives, including those present in pooled funds and forward starting transactions, will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

12.3 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

13. Providing for Debt Repayment - 2017/18 Minimum Revenue Provision Statement

13.1 The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (SI 2008/414) place a duty on local authorities to make a prudent provision for debt redemption. Guidance on this MRP has been issued by the Secretary of State and local authorities are required to "have regard" to such Guidance under section 21(1A) of the Local Government Act 2003.

13.2 The four MRP options available are:

Option 1: Regulatory Method	Option 2: CFR Method
Option 3: Asset Life Method	Option 4: Depreciation Method

13.3 Options 1 and 2 may be used only for supported non-HRA capital expenditure (ie where the Government supports the cost of financing new borrowing through a recurring grant). Methods of making prudent provision for self financed non-HRA capital expenditure include Options 3 and 4 (which may also be used for supported expenditure if the Council chooses). There is no requirement to charge MRP in respect of HRA capital expenditure funded from borrowing.

13.4 The MRP Statement will be submitted to Council before the start of the financial year. If it is ever proposed to vary the terms of the original MRP Statement during the year, a revised statement will be put to Council at that time.

13.5 The Council's Policy for making a MRP in 2017/2018 will be:

- *capital expenditure incurred before 1 April 2008:* MRP will be provided at an approximate reduction of 4% in the CFR
- *capital expenditure which is supported by recurring revenue grants or contributions:* there is no expectation that the Council will incur this type of expenditure in 2017/2018, but if so Option 1 will apply – MRP will be equal to the amount determined in accordance with the former regulations 28 and 29 of the Local Authorities Capital Finance and Accounting (England) Regulations 2003 as if they had not been revoked
- *capital expenditure incurred for development or asset realisation purposes:* where capital expenditure is incurred in respect of a project which is intended to unlock future capital receipts (eg the refurbishment of a building ahead of its sale, the acquisition of sites associated with the North Street Development) no MRP will be

provided, the expectation being that the increase in CFR will subsequently be offset by use of the eventual receipts

- *capital expenditure on commercial investment property:* where capital expenditure is incurred on the acquisition, construction or improvement of land and buildings with the intention of generating a recurring income stream, no MRP will be provided. Any such projects will have been evaluated prior to commencement to ensure that it provides a positive annual long-term return after allowing for interest costs and notional repayment of principal
- *any other capital expenditure:* Option 3 will apply – MRP will be calculated according to the asset life method and will be made in equal instalments over the life of the asset.

13.6 The Housing Revenue Account 30-year Business Plan includes the principle that the long-term borrowing required on the move to self-financing will be repaid at the earliest opportunity. However, there is no requirement to do so and become 'debt-free'. In order to maintain flexibility, resources will be set aside in the HRA balance for potential debt repayment, but formal Revenue Provisions (which cannot be reversed) will not be made other than to reduce internal borrowing from the General Fund.

14. Reporting on the Treasury Outturn

The Deputy Chief Executive will report on Treasury Management activity/performance as follows:

Report to/Coverage	Frequency:
Council	
Treasury Management Strategy/Annual Investment Strategy/MRP Policy	Annually before start of the year
Treasury Management Strategy/Annual Investment Strategy/MRP Policy – mid year report	Annually mid year
Treasury Outturn report	Annually after year end and by 30 September
Cabinet	
Receives each of the above reports in advance of Council and makes recommendations as appropriate	In advance of year/mid-year/after year end and by 30 September
Receives confirmation that Treasury transactions have complied with Strategy and benchmark performance information	As part of Quarterly Financial Performance reports.
Audit and Standards Committee	
Receives each of the above reports in advance of Cabinet (where publication timetable permits) and makes observations as appropriate	In advance of year/mid-year/after year end and by 30 September
Reviews details of Treasury transactions against Strategy and makes observations to Cabinet	Every cycle

15. Training

15.1 The TM Code requires the Deputy Chief Executive, as responsible officer, to ensure that all councillors tasked with Treasury Management responsibilities, including scrutiny of the Treasury Management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. Arlingclose will be asked to continue the briefing programme for Councillors which has been running since 2009.

15.2 The training needs of the Council's Treasury Management staff will be reviewed as part of the annual corporate staff appraisal/training needs assessment process for all Council employees. The Council's contract with Arlingclose includes provision for staff to attend training seminars and workshops.

16. Investment Consultants

16.1 The Council appointed Arlingclose as its financial advisers for the period 1 July 2012 to 30 June 2016, with an option to extend for a further year at the discretion of the Council. The Council exercised the option to extend this agreement, which will now come to an end on 30 June 2017.

16.2 Until the end of its contract period, Arlingclose will be the Council's primary source of information, advice and assistance relating to investment activity. Individual investment decisions are made by the Council. Review meetings are held at least twice a year, at which the quality of the service received to date is discussed.

16.3 In late 2016, the East Sussex Procurement Hub (lead authority Wealden District Council) conducted a joint procurement for treasury management services on behalf of all East Sussex district and borough councils, in response to which Arlingclose submitted the most economically advantageous tender. As a result, the Council will be able to appoint Arlingclose for a further four years from June 2017. The final decision whether to do so will be made in conjunction with Eastbourne Borough Council given that a shared finance team (with treasury management responsibility) is expected to be established in 2017.

17. Publication

The Annual Treasury Management Statement and Investment Strategy, along with any in-year revisions, can be downloaded from www.lewes.gov.uk and is also available on request to the Director of Corporate Services, Southover House, Southover Road, Lewes, or by email to finance@lewes.gov.uk.

Appendix A - Arlingclose's Economic and Interest Rate Forecast

	Mar-17	Jun-17	Sep-17	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.13**
Arlingclose Central Case	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**	**0.25**
Downside risk	-0.25	-0.25	-0.25	-0.25	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.42**
3-month LIBID rate														
Upside risk	0.05	0.10	0.10	0.10	0.15	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	**0.19**
Arlingclose Central Case	**0.25**	**0.25**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.30**	**0.29**
Downside risk	-0.25	-0.25	-0.25	-0.30	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	-0.40	**-0.36**
1-yr LIBID rate														
Upside risk	0.10	0.15	0.15	0.15	0.20	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	**0.24**
Arlingclose Central Case	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.50**	**0.60**	**0.70**	**0.85**	**0.90**	**0.90**	**0.90**	**0.95**	**0.68**
Downside risk	-0.15	-0.15	-0.15	-0.20	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	-0.30	**-0.26**
5-yr gilt yield														
Upside risk	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.40**
Arlingclose Central Case	**0.50**	**0.45**	**0.45**	**0.45**	**0.50**	**0.50**	**0.50**	**0.55**	**0.60**	**0.65**	**0.70**	**0.75**	**0.80**	**0.57**
Downside risk	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.48**
10-yr gilt yield														
Upside risk	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.40**
Arlingclose Central Case	**0.95**	**0.90**	**0.90**	**0.90**	**0.95**	**0.95**	**0.95**	**1.00**	**1.05**	**1.10**	**1.15**	**1.20**	**1.25**	**1.02**
Downside risk	-0.45	-0.45	-0.45	-0.45	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	**-0.48**
20-yr gilt yield														
Upside risk	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.40**
Arlingclose Central Case	**1.50**	**1.45**	**1.45**	**1.45**	**1.50**	**1.50**	**1.50**	**1.55**	**1.60**	**1.65**	**1.70**	**1.75**	**1.80**	**1.57**
Downside risk	-0.55	-0.55	-0.55	-0.55	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	**-0.58**
50-yr gilt yield														
Upside risk	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	0.40	**0.40**
Arlingclose Central Case	**1.40**	**1.35**	**1.35**	**1.35**	**1.40**	**1.40**	**1.40**	**1.45**	**1.50**	**1.55**	**1.60**	**1.65**	**1.70**	**1.47**
Downside risk	-0.55	-0.55	-0.55	-0.55	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	-0.60	**-0.58**

Underlying assumptions:

- The medium term outlook for the UK economy is dominated by the negotiations to leave the EU. The long-term position of the UK economy will be largely dependent on the agreements the government is able to secure with the EU and other countries.
- The global environment is also riddled with uncertainty, with repercussions for financial market volatility and long-term interest rates. Donald Trump's

victory in the US general election and Brexit are symptomatic of the popular disaffection with globalisation trends. At the moment financial markets appear to be expecting stronger global growth, but the potential rise in protectionism could dampen global growth prospects and therefore inflation. However, following significant global fiscal and monetary stimulus, the short term outlook for the global economy is somewhat brighter than earlier in the year. US fiscal stimulus is also a possibility following Trump's victory.

- Recent data present a more positive picture for the post-Referendum UK economy than predicted due to continued strong household spending.
- Over the medium term, economic and political uncertainty will likely dampen investment intentions and tighten credit availability, prompting lower activity levels and potentially a rise in unemployment.
- The currency-led rise in CPI inflation (currently 1.2% year/year) will continue, breaching the target in 2017, which will act to slow real growth in household spending due to muted or negative real wage growth.
- The depreciation in sterling will, however, assist the economy to rebalance away from spending. The usual negative contribution from net trade to GDP growth is likely to diminish, largely due to weaker domestic demand. Export volumes will increase marginally.
- Given the pressure on household spending and business investment, the rise in inflation is highly unlikely to prompt monetary tightening by the Bank of England, with policymakers looking through import-led CPI spikes to the negative effects of Brexit on economic activity and, ultimately, inflation.
- Bank of England policymakers have, however, highlighted that excessive levels of inflation will not be tolerated for sustained periods. Given this view and the current inflation outlook, further monetary loosening looks less likely.

Forecast:

- Globally, the outlook is uncertain and risks remain weighted to the downside. The UK domestic outlook is uncertain, but likely to be weaker in the short term than previously expected.
- The likely path for Bank Rate is weighted to the downside. The Arlingclose central case is for Bank Rate to remain at 0.25%, but there is a 25% possibility of a drop to close to zero, with a very small chance of a reduction below zero.
- Gilt yields have risen sharply, but remain at low levels. The Arlingclose central case is for yields to decline when the government triggers Article 50.

Appendix B – Prudential Indicators 2017/2018 to 2019/2020 – NOT PART OF AUDIT AND STANDARDS COMMITTEE REVIEW

1. Background:

There is a requirement under the Local Government Act 2003 for local authorities to have regard to CIPFA's Prudential Code for Capital Finance in Local Authorities (the "CIPFA Prudential Code") when setting and reviewing their Prudential Indicators. Some of the Prudential Indicators relate directly to the Council's Capital Programme and are considered by Cabinet when the Capital Programme is set. These Indicators are also included below for completeness of reporting.

Appendix C – Approved Investment Counterparties and Limits

Credit Rating	Banks Unsecured	Banks Secured	Government	Corporates	Registered Providers
UK Govt	n/a	n/a	£ Unlimited 50 years	n/a	n/a
AAA	£2m 5 years	£2m 20 years	£2m 50 years	£2m 20 years	£2m 20 years
AA+	£2m 5 years	£2m 10 years	£2m 25 years	£2m 10 years	£2m 10 years
AA	£2m 4 years	£2m 5 years	£2m 15 years	£2m 5 years	£2m 10 years
AA-	£2m 3 years	£2m 4 years	£2m 10 years	£2m 4 years	£2m 10 years
A+	£2m 2 years	£2m 3 years	£2m 5 years	£2m 3 years	£2m 5 years
A	£2m 13 months	£2m 2 years	£2m 5 years	£2m 2 years	£2m 5 years
A-	£2m 6 months	£2m 13 months	£2m 5 years	£2m 13 months	£2m 5 years
BBB+	£1m 100 days	£1m 6 months	£1m 5 years	£1m 6 months	£1m 2 years
Pooled funds	£3m per fund				
Note - Unsecured investment (restricted to overnight deposits only) with a bank rated BBB or below will be permissible in the case of the Council's current account bank in the event that it is rated at that level.					

Further details of the counterparty types shown in the table above are as follows:

Banks Unsecured: Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail.

Banks Secured: Covered bonds, reverse repurchase agreements and other collateralised arrangements with banks and building societies. These investments are secured on the bank's assets, which limits the potential losses in the unlikely event of insolvency, and means that they are exempt from bail-in. Where there is no investment specific credit rating, but the collateral upon which the investment is secured has a credit rating, the highest of the collateral credit rating and the counterparty credit rating will be used to determine cash and time limits. The combined secured and unsecured investments in any one bank will not exceed the cash limit for secured investments.

Government: Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

Corporates: Loans and bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

Registered Providers: Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain the likelihood of receiving government support if needed.

Pooled Funds: Shares in diversified investment vehicles consisting of any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Short-term Money Market Funds that offer same-day liquidity and very low or no volatility will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

Bond, equity and property funds offer enhanced returns over the longer term, but are more volatile in the short term. These allow the Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. Because these funds have no defined maturity date, but are available for withdrawal after a notice period, their performance and continued suitability in meeting the Council's investment objectives will be monitored regularly.

Glossary of Treasury Management Terms

Affordable Borrowing Limit	Each local authority is required by statute to determine and keep under review how much money it can afford to borrow. The Prudential Code (see below) sets out how affordability is to be measured.
Bank Rate	The main interest rate in the economy, set by the Bank Of England, upon which others rates are based.
Basis Point	A convenient way of measuring an interest rate (or its movement). It represents 1/100th of a percentage point, ie 100 basis points make up 1%, and 250 basis points are 2.5%. It is easier to talk about 30 basis points than "point three of one per cent".
Bonds	Debt instruments issued by government, multinational companies, banks and multilateral development banks. Interest is paid by the issuer to the bond holder at regular pre-agreed periods. The repayment date of the principal is set at the outset.
Capital Expenditure	Spending on the purchase, major repair, or improvement of assets eg buildings and vehicles
Capital Financing Requirement (CFR)	Calculated in accordance with government regulations, the CFR represents the amount of Capital Expenditure that it has incurred over the years and which has not yet been funded from capital receipts, grants or other forms of income. It represents the Council's underlying need to borrow.
Certificate of Deposit	A short-term marketable financial instrument typically issued for periods of less than six months by banks and building societies. Interest can be at a fixed or variable rate.
Chartered Institute of Public Finance and Accountancy (CIPFA)	CIPFA is one of the leading professional accountancy bodies in the UK and the only one that specialises in the public services. It is responsible for the education and training of professional accountants and for their regulation through the setting and monitoring of professional standards. CIPFA has responsibility for setting accounting standards for local government.
Counterparty	Institution with which the Council may make an investment
Credit Default Swaps	CDS are a financial instrument for swapping the risk of debt default and are effectively an insurance premium. Local authorities do not trade in CDS but trends in CDS prices can be monitored as an indicator of relative confidence about the credit risk of counterparties.
Credit Rating	A credit rating is an independent assessment of the credit quality of an institution made by an organisation known as a rating agency. The rating agencies take many factors into consideration when forming their view of the likelihood that an institution will default on their obligations, including the institution's willingness and ability to repay. The ratings awarded typically cover the short term outlook, the long term outlook, as well as an assessment of the extent to which the parent company or the state will honour any obligations. The three main agencies providing credit rating services are Fitch Ratings, Moody's and Standard and Poor's.

Fixed Deposits	Loans to institutions which are for a fixed period at a fixed rate of interest
Gilts	These are issued by the UK government in order to finance public expenditure. Gilts are generally issued for set periods and pay a fixed rate of interest. During the life of a gilt it will be traded at price decided in the market.
Housing Revenue Account (HRA)	There is a statutory requirement for local authorities to account separately for expenditure incurred and income received in respect of the dwellings that they own and manage.
Internal Borrowing	The temporary use of surplus cash which would otherwise be invested, as an alternative to borrowing from the PWLB or a bank in order to meet the cost of capital expenditure.
LIBID	The rate of interest at which first-class banks in London will bid for deposit funds
Minimum Revenue Provision (MRP)	The minimum amount which must be charged to an authority's revenue account each year and set aside as provision for the repayment of debt.
Operational boundary	This is the most likely, prudent view of the level of gross external indebtedness. A temporary breach of the operational boundary is not significant.
Prudential Code/Prudential Indicators	The level of capital expenditure by local authorities is not rationed by central government. Instead the level is set by local authorities, providing it is within the limits of affordability and prudence they set themselves. The Prudential Code sets out the indicators to be used and the factors to be taken into account when setting these limits
Public Works Loan Board (PWLB)	A central government agency which provides long- and medium-term loans to local authorities at interest rates only slightly higher than those at which the Government itself can borrow.
Treasury Management Strategy Statement (TMSS)	Approved each year, this document sets out the strategy that the Council will follow in respect of investments and financing both in the forthcoming financial year and the following two years.
Treasury Bills (T-Bills)	These are issued by the UK Government as part of the Debt Management Office's cash management operations. They do not pay interest but are issued at a discount and are redeemed at par. T-Bills have up to 12 months maturity when first issued.