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, 27 November 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.

15/11/2017

Catherine Knight
Assistant Director of Legal and Democratic Services

Agenda

1 **Committee Membership 2017/2018**
To note the appointment of Councillor Johnny Denis on the Audit and Standards Committee membership in place of Councillor Tony Rowell for the remainder of the current municipal year.

2 **Minutes**
To approve the Minutes of the meeting held on 25 September 2017 (copy previously circulated).

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

4 **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.

5 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.

6 Written Questions

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

7 Interim Report on the Council's Systems of Internal Control 2017/18 (page 3)

To receive the Report of the Head of Audit and Counter Fraud (Report No 167/17 herewith)

8 Treasury Management (page 19)

To consider the Report of the Deputy Chief Executive (Report No 168/17 herewith)

9 Annual Audit Letter - Audit for the year ended 31 March 2017 (page 41)

To consider the Report of BDO Accountants and Business Advisers (Report No 169/17 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, 22 January 2018 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, J Denis, N Enever, S Gauntlett, A Loraine and R O'Keeffe

(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-eastbourne.gov.uk)

Agenda Item No:	**7**	**Report No:**	**167/17**
Report Title:	**Interim Report on the Council's Systems of Internal Control 2017/18**		
Report To:	**Audit and Standards Committee**	**Date: 27 November 2017**	
Ward(s) Affected:	**All**		
Report By:	**Head of Audit and Counter Fraud**		

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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 seven months of 2017/18, 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 seven months of 2017/18 (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 first applied from 1 April 2013. The PSIAS have been updated, with new standards published in March 2017. The new standards are not materially different from the previous version, and so have not been separately reported to the Committee.

2.2 The PSIAS 2017 continue to specify the requirements for the reporting to the Audit and Standards Committee and senior management by Head of Audit and Counter

Fraud (HACF). These requirements are met via a series of reports, including interim reports to each meeting of the Committee.

2.3 Each interim report includes a review of the work undertaken by Internal Audit compared to the annual programme, an opinion of HACF 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.

2.4 In September 2015, Cabinet approved a strategy for the development of shared services between Lewes District Council (LDC) and Eastbourne Borough Council (EBC) based on the integration of the majority of council services via a Joint Transformation Programme (JTP). The formal integration of the Internal Audit and Counter Fraud Teams in both councils took place on 1 July 2017.

3 Internal Control Environment at Lewes District Council

3.1 The Annual Report on the Council's Systems of Internal Control for 2016/17 included the opinion of HACF 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 seven 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.

4 Internal Audit work 2017/18

4.1 Table 1 shows that a total of 292 audit days have been undertaken compared to 363 days planned in the first seven months of the year.

Table 1: Plan audit days compared to actual audit days for April to October 2017

Audit Area	Actual audit days for the year 2016/17	Plan audit days for the year 2017/18	Actual audit days to date	Pro rata plan audit days to date
Main Systems	347	295	177	
Central Systems	83	65	32	
Departmental Systems	86	65	1	
Performance and Management Scrutiny	8	45	15	
Computer Audit	2	5	4	
Management Responsibilities/Unplanned Audits	113	147	63	
Total	639	622	292	363

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.

The variance of 71 days has arisen mainly from the retirement of the Senior Auditor in January 2017, with the vacancy filled on 4 September 2017, and the additional time being spent on management tasks arising from the JTP. It is estimated that the audit days will be closer to plan by the year end.

4.2 This section of the report summarises the work undertaken by Internal Audit, compared to the annual plan that was presented to the Audit and Standards Committee in March 2017. Further information on each of the audits completed since the previous meeting of the Committee is given at Appendix A1.

4.3 ***Main Systems:*** The main work has been 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 2016/17. A final report has been issued, together with a separate final report on the issues arising from the review of Non-Domestic Rates (NDR).

4.4 The work on behalf of BDO to test the Council's HB subsidy claim 2015/16 was completed, and the audited claim submitted, during July 2017. 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 and the initial additional testing were completed in late September. The timetabled date for BDO to have signed off and submitted the audited claim was at the end of November 2016, but that date was not met because of the extra work that was required. This included further additional testing, reperformance by BDO, and the resolution of queries and challenges. The overall value of the claim was £36.5m. In July 2017, DWP confirmed the results of the audit - there had been an overpayment of subsidy of £6,976, but with a related understatement of £2,367 the net effect was a recovery of £4,609 by DWP.

4.5 The work on the HB subsidy claim for 2016/17 is underway. BDO have identified the need for significant additional testing to address the issues noted in the 2015/16 claim. The timetabled date for BDO to sign off and submit the audited claim is the end of November 2017, but it is likely that the audited claim will not be submitted before the end of February 2018.

4.6 In order to avoid similar delays in the completion of the audit of the HB subsidy claim for 2017/18, Internal Audit assisted operational managers to engage external consultants Branch and Lee to carry out data analysis of the HB files. Branch and Lee have performed a similar service for EBC for the last two years, and this has been shown to have positive impacts on the records of HB claims ahead of the formal audit. Branch and Lee reported their results on 14 November 2017, and service managers are assessing the potential need for training and revised procedures to address the issues raised in the report.

4.7 ***Central Systems:*** A draft report has been prepared for the audit of Ethics, with the work having been done by the Audit Manager at EBC. A final report has been issued for a review of EBC/LDC compliance with aspects of the Regulatory Powers Act (RIPA), and a similar review of compliance with the General Data Protection Regulation (GDPR) at both councils is at the draft report stage. HACF has carried out an independent consultancy review of options for the future management of the Lewes and Eastbourne Leisure Trusts – the results of the review are summarised at Appendix A1.

4.8 ***Departmental Systems:*** The audit of Estates Management, incorporating work on the corresponding function at EBC, began in January 2017 but was put on hold to free resources for the work on the HB subsidy claim 2015/16 and the testing of the major financial systems – the audit will recommence as soon as resources become available. An audit of the procedures for managing the Housing Register is at the initial planning stage.

4.9 ***Performance and Management Scrutiny:*** The main work in this category has been in reviewing the data that supports the Annual Governance Statement (AGS) for 2017.

4.10 ***Computer Audit:*** Internal Audit has examined the IT aspects of the main financial systems (see 4.3 above).

4.11 ***Management Responsibilities/Unplanned Audits:*** This category provides resources for activities such as support for the Audit and Standards Committee, managing the Counter Fraud Team, liaison with BDO, managing the Follow Up procedures, as well as for special projects or investigations.

4.12 HACF has carried out an independent consultancy review of the options for the future management of strategic procurement at both councils. A report has been considered by CMT, and a summary of the review results is included at Appendix A1. A review of the Prevent and Protect Strategy – also being carried out by HACF – is underway.

4.13 Internal Audit continues to coordinate the Council's work on NFI data matching exercises. Internal Audit, the Investigations Team and service managers prepared for the receipt of the reported matches, and nominated officers to investigate matches in their service areas. The reported matches arrived in late January 2017 - there are over 2,000 separate matches detailed across 93 reports. Each report sets out different types of potential frauds among benefit claimants, housing tenants, and anyone receiving payments or discounts from the Council. The exercise involves analysis of the matches to identify those that are the result of error or coincidence, and then the examination of the remaining matches to assess the likelihood of fraud - 335 matches have been examined, with no fraud or error noted so far. The Audit and Standards Committee will be kept advised of progress.

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 2017/18 has been on confirming the implementation of the recommendations that had been agreed in the previous year.

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 2016/17 were reported to the June meeting of the Audit and Standards Committee. The results enabled the HACF 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 Audit and Standards Committee.

7 Combatting Fraud and Corruption

Local initiatives

7.1 The Counter Fraud Team is a member 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.

7.2 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. The Hub is managed by officers at EBC with input from ESFOG partners. Recent Hub activities have included a shared approach to publicity for Hub activities and the development of an on-line system to allow the public to report suspected frauds – the Counter Fraud Teams at EBC and LDC will use a shared web link to receive these reports.

LDC Counter Fraud Team

7.3 At present, countering housing tenancy fraud and abandonment, and preventing RTB fraud, are the main operational priorities for the Counter Fraud Team because of the evidence of this being a high risk area for the Council. There are 15 cases of suspected abandonment and/or subletting under investigation, plus one of suspected housing application fraud. Three properties have been returned to stock after cases of abandonment. Further property returns are anticipated in current cases where evidence gives a strong indication that the tenant no longer lives at the property. Three cases of suspected RTB fraud are being investigated, and 18 RTB applications have been withdrawn since April 2017 after intervention by the team. The team will assess the withdrawn applications to determine whether the cases indicate potential fraud.

7.4 Recent months have seen a number of case referrals that have required extensive liaison with a range of Council services and external agencies to protect residents and prevent fraud. The team will be working further with front line staff to help in recognising possible issues such as attempted identity fraud.

7.5 Internal Audit has in place an agreement with DWP for the management of cases of HB fraud. The major work on each HB case is the responsibility of the national Single Fraud Investigation Service (SFIS) within DWP. LDC retains a role in referring cases of suspected HB fraud to SFIS and handling requests for information. In an agreement with Counter Fraud colleagues at EBC, a member of that team carries out the DWP liaison work for LDC and thus allows the LDC team to focus on case work in other areas. In the period since April 2017, there have been twelve referrals to SFIS, and 58 information requests have been actioned.

7.6 NDR is the development priority for the team, based upon initial research, training and a pilot study in 2016. The team will revisit the risk assessment for NDR to determine the impact of recent government announcements on NDR, and the possible effect on rate reliefs to small businesses. The aim is to have a coordinated exercise to counter business rates fraud across the county, using a methodology developed with Hub partners.

8 Risk Management

8.1 Cabinet approved the Risk Management Strategy in September 2003. Since then risk management at the Council has been developed via a series of action plans, 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.

8.2 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.

8.3 In response to reductions in Government funding for local authorities, the Council has been making significant savings each year in its General Fund budget (which covers all services except the management and maintenance of Council owned homes) since 2011/12.

8.4 The General Fund savings continue to be required over the next four years, with net expenditure to reduce by £2.2m, from £13.2m to £11.0m by 2020/21. The savings target for 2017/18 is £0.6m, half of which is to come from the continuing Joint Transformation Programme (JTP) with EBC. This target is expected to be achieved although the realization of some of the JTP saving is likely to be deferred, reflecting the timing of key phases of the programme.

8.5 There are also pressures to reduce spending on the management and maintenance of Council owned (HRA) housing. Starting in 2016/17, the Government has required all housing authorities to reduce tenants' rents by a 1% in cash terms in each of the four years through to 2019/20. As a result, by 2019/20, total annual rent income will have fallen by £0.6m to £14.4m. This means that savings of £2.2m will be needed to offset the expected impact of inflation on expenditure budgets over that period. A share of the JTP savings will pass through to the HRA.

9 System of management assurance

9.1 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 2016/17. At its meeting on 30 May 2017 CMT confirmed that there were no significant governance issues to report, and there has been nothing in the first seven months of the financial year to change these assessments.

10 Corporate governance

10.1 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 AGS for 2017 was presented to the June 2017 meeting of the Committee – a version of that AGS with minor amendments was issued with the financial statements for 2016/17.

11 External assurance

11.1 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 Council's current external auditors are BDO, and the results of their external reviews have helped inform the opinion on the internal control environment. The recent results are summarised below.

11.2 Audit Completion Report (September 2017) – This interim report summarised the key issues from the audit work carried out by BDO for the year ending 31 March 2017, and was presented to the September 2017 meeting of the Committee. The key issues were:

- Subject to the successful resolution of outstanding matters in respect of two property additions and potential errors in Housing Benefit testing, which are largely procedural, BDO anticipate issuing an unmodified opinion on the financial statements for the period ended 31 March 2017.
- BDO identified a number of immaterial misstatements, but these were found to have no impact on the value of net assets or the surplus on provision of services.
- BDO did not identify any significant deficiencies in internal controls.
- BDO have no exceptions to report in relation to the consistency of the Annual Governance Statement (AGS) with the financial statements or other knowledge.
- BDO anticipate issuing an unmodified opinion on the Council's use of resources.
- BDO noted that the Council has appropriate arrangements to remain financially sustainable over a period of the Medium Term Financial Strategy (MTFS). All of the required savings for 2017/18 have been identified.
- BDO noted that the Council's Whole of Government Accounts (WGA) submission is below the threshold for further work other than to submit the WGA Assurance Statement - the relevant section of the statement would be submitted prior to the statutory deadline.
- BDO noted that the Council had made progress against all the recommendations that were raised in respect of the New Homes Project, and there is evidence that the learning from this project has been applied to other capital projects.

12 Future external audit arrangements

12.1 Under the provisions of the Local Audit and Accountability Act 2014, the Secretary of State for Communities and Local Government has specified that a company, Public Sector Audit Appointments (PSAA) Limited, will appoint auditors to local government, police and some NHS bodies.

12.2 The Council has opted into the PSAA arrangements, and has recently been consulted on the appointment of the external auditor for the period of five years from 2018/19. PSAA have appointed Deloitte LLP, and the Council has responded to the consultation to confirm its acceptance of the appointment, which will start on 1 April 2018. Deloitte LLP will also be the external auditors for EBC.

12.3 BDO will carry out the audits of the 2017/18 accounts and the 2017/18 HB subsidy claim, and will therefore be working with the Council until at least November 2018.

13 Financial Appraisal

13.1 There are no additional financial implications from this report.

14 Sustainability Implications

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

15 Risk Management Implications

15.1 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.

16 Legal Implications

16.1 There are no legal implications arising from this report.

17 Equality Screening

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

18 Background Papers

2017/18 Annual Audit Plan

19 Appendices

19.1 Appendix A1 - Statement of Internal Audit work and key issues.

19.2 Appendix A2 - Table of abbreviations.

19.3 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: Review of governance and options for the future management of the Lewes and Eastbourne Leisure Trusts

Date of issue: November 2016

This review was commissioned by the Chief Executive to advise on the governance and future options for the management of the leisure trusts, focusing on the potential to combine the services. The key findings were:

Community leisure services are discretionary, and as such councils do not have to provide them. Both EBC (2004) and LDC (2006) chose to adopt an enabling model that allowed most or all of their leisure services to be put under trust status. The current review identified that there is scope for improvements in the way that the leisure services can be managed and there are a number of options for how those services can be provided jointly.

There are significant variations in the way the trusts operate. These include differences in organisational structures, financing arrangements, the scale of facilities operated, the arrangements for maintenance of the buildings, and the oversight and governance by each council. These differences are due to the way the trusts were set up and the different objectives for leisure services at the two councils.

The review identified areas for potential improvement in some performance and governance information. The review concluded that, if a decision is made to combine the services, consideration should be given to combining the best of the current arrangements from each trust.

Seven options for the future delivery of a combined managed leisure service were identified, with four options being considered as potentially viable. These were:

- Create one new trust for both EBC and LDC;
- Outsource to a leisure services trust (private sector) for both councils;
- Outsource to an existing trust (not for profit) for both councils; and
- Establish a Teckal[1] company for LDC and EBC leisure services.

Senior management was asked to consider the four options for the future management of the two trusts. If the decision is that services are not to be jointly managed then there are a number of similar options for EBC to manage its leisure services in future.

Following the review, management has considered the procurement implications of the various options, as follows:

- The nature of the management structure chosen will affect the way in which leisure

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[1] Most Local Authority Trading Companies (LATCs) begin with a period where contracts are awarded directly. This allows them time to increase their commerciality before entering markets that are more competitive. The so-called Teckal exemption allows councils to award contracts directly to LATCs and gives the company freedom to trade commercially for up to 20% of its turnover. Both the council and the company need to have clarity in this area.

services might be procured. Any decision to outsource leisure services to an external provider under a contractual arrangement for the provision of leisure services will require the councils to undertake a public procurement exercise, so opening up the service provision to competition. This will be the case, irrespective of whether the arrangement is structured as a services contract or a services concession contract under EU regulations.

- Use of a Teckal company owned by EBC and /or LDC would not require competition through a public procurement exercise.
- There is one further suggestion which the councils might wish to consider. The councils could enter an arrangement which does not create a services contract under the public procurement regulations. Typically, this would involve the grant of a lease of the council's premises to a leisure operator with NO binding service obligations. The lease itself would determine the user of the premises i.e. use restricted to leisure and closely related ancillary activities. There would be no binding obligation on the lessee to provide services under any sort of service level agreement. However, it would be possible to create incentives for the operator to meet prescribed council targets in return for which the operator might receive a grant from the councils. It would also be possible to enter specific contracts to ensure the provision of certain services provided they were below the EU Threshold which would require a procurement exercise. In the event of a lease being granted, our own Contract Procedure Rules (at both EBC and LDC) would usually require a form of invitation to tender/expressions of interest and advertisement in those cases where the estimated rent is likely to exceed £25,000 per annum. However, Cabinet does have the power to decide to waive this rule in any particular case if it believes there is good reason to do so.

This summary of the review findings has not been previously reported to the Audit and Standards Committee as the decision on the future direction of the leisure trusts remains under consideration. Significant time has elapsed since the results of the review were reported to CMT, and with no decision yet reached the HACF is now reporting the key findings of the review to the Committee.

Audit Report: Review of options for the future management and location of strategic procurement at Eastbourne Borough Council (EBC) and Lewes District Council (LDC)

Date of issue: June 2017

This review was commissioned by the Chief Executive to examine the current arrangements for strategic procurement and the options for its future delivery at EBC and LDC.

Strategic procurement is an essential part of the work by councils to improve the way they acquire goods, services and works whilst at the same time identifying savings and ensuring best value. It embraces all activities within the procurement cycle from specification to receipt and payment, and provides a planned approach to procurement that is aligned to the councils' corporate priorities. Operational procurement focuses on the day to day acquisition of goods, works and services.

EBC and LDC between them procure in the region of £50 million in goods, services and works each year. This represents a substantial proportion of the councils' budgets. Best practice recommends that there is a strong focus on strategic procurement. The LDC and EBC Joint Transformation Programme (JTP) has given an opportunity for the re-evaluation of the role of strategic procurement and consideration as to where this might sit within the councils' shared services. The following key issues were identified in the review:

- The staff resources available for strategic procurement have been reduced by 0.4 FTE at EBC and LDC. In addition, strategic procurement resources have been reduced by a further 0.2 FTE because of the end of the Improvement and Efficiency South East (IESE) contract. The impact of these changes is that that there is currently limited focus on strategic procurement tasks.

- The state of readiness for effective strategic procurement is reasonable in a number of areas. However, in other areas there is scope for significant improvement.

- Detailed spend analysis is a key tool for identifying opportunities for improved procurement methods and savings.

- The number and value of the contracts that are coming up for renewal from 2018/19 onwards are significant. Work will need to start on the renewals process in the current year, and similar efforts will be required in following years. This renewal process will give officers an opportunity to consider how these services might be provided in the future.

- A review of good practice in district and borough councils has noted that there has been a focus on the sharing of procurement resources either through a shared service arrangement or a procurement hub led by one authority.

- There are three realistic options for the future location of the strategic procurement function. These options are transferring the function to the East Sussex Procurement Hub (ESPH), locating it in Legal Services or locating it in Property and Facilities. It is the opinion of HACF that all of the options would require additional specialist resources to ensure the effective management of strategic procurement. It estimated that at least an additional one FTE is required for this function if it remains within the two councils. If this function were to be transferred to the Hub there could be a significant increase in costs for EBC and LDC.

- The National Procurement Strategy (NPS) represents the "gold standard" that councils are aiming to achieve in the management of procurement. Neither LDC of EBC have currently assessed where they currently stand against this standard.

As a result of the review, CMT has agreed that strategic procurement should be under the control of the Director of Regeneration and Planning. The strategic procurement role has been delegated to the recently appointed Head of Commercial Business, who will develop the strategic procurement arrangements at the councils over the coming year, taking into account the findings of this review.

Audit Report: Key Financial Systems 2016/17

Date of issue: 4 October 2017

Overall opinion:

The audit has confirmed that procedures and controls within the key systems are operating to a reasonable standard in most respects. The audit has not identified any significant control issues that will have an impact on the Council's main accounts.

In a number of cases the controls over ordering and the receiving of goods and services have not operated as intended, or are not operated consistently across the Council. These issues reflect a situation in which lists of authorised signatories and the operation of other controls appear unable to keep pace with changes in staffing and officers' responsibilities. In other areas, particularly the write off of debts, established procedures have not operated as originally planned. These issues are not considered likely to have a material effect on the integrity of the main accounts but the issues themselves indicate a change in the control environment within the Finance team and service areas in response to new structures at the Council. On balance, the control environment is appropriate to the Council's requirements in all significant respects.

This review, which supplements the other work of Internal Audit, enables HACF to form an opinion on the Council's control environment for the purposes of the Annual Governance Statement (AGS). BDO uses the results of this review to gain assurance about the systems operated by the Council and the effectiveness of the controls that are applied.

The report contains summaries of the findings for the twelve key systems. The findings from the audit of NDR justified a separate report as shown below.

Audit Report: Non Domestic Rates (NDR)

Date of final issue: 4 October 2017

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 NDR. Controls are in place and to an extent there is reasonable compliance.

For example, effective procedures are in place to ensure that authorised updates to the NDR database are made regularly. Each application for Charitable Relief examined during the audit was supported by an application requesting relief and the relief was calculated correctly. Income is processed through the ICON receipting system and the reconciliation between the receipting system and Academy is completed weekly. Refunds are authorised correctly, and automatic arrears and recovery processes are in place within the Academy system, with Liability Orders automatically produced when an account is in default and progression to bailiff action a standard approach for accounts in arrears.

However, there are gaps in the control processes which weaken the system, and there is a need to consider action to reduce the risk to the Council. The report contained four recommendations.

Main points:

Empty Property Relief (EPR)

EPR is granted when a business notifies the Council that it has vacated its premises. The period of the relief varies, but the standard length of time is three months which is extended to six months in the case of certain industrial properties. After this period, the full amount of NDR is payable.

In the sample of business properties selected for review, the empty property relief was calculated correctly but there was limited evidence to support the decision to award the relief. None of the empty properties in the sample had been inspected and the log of inspections was not up to date. There were 216 empty properties recorded on Academy at 31 March 2017; of these 58 attract an exemption from business rates, and a further 66 are exempt because they have an RV below £2,600. It is not possible to confirm the status of the remaining properties recorded as empty, and there is the potential for empty property relief to be incorrectly claimed by businesses across the District.

Small Business Rate Relief (SBRR)

The audit confirmed that there is evidence to support the award of the Small Business Rate Relief (SBRR) claimed by the ten NDR accounts examined. SBRR was calculated correctly in each case, which was supported by an application form, and the rateable value was verified by checks to the Valuation Office (VO) listing. However, the standard checks to highlight potentially fraudulent SBRR claims would not be sufficient to identify all circumstances in which businesses understate the number of premises that are in operation.

Write-offs

Five write-offs exceed £10,000. These included three which had arisen as a result of bankruptcy/insolvency proceedings, and two had been due to delays in identifying the person responsible for NDR at the premises. It appears likely that a more effective inspection regime would have increased the chances of identifying the owner of two premises mentioned above, and would have made it more difficult for the business owners to deny liability.

The write-offs that exceeded £10,000 were not subject to the reporting and/or authorisation processes required by Financial Procedure Rules.

Audit Report: Interim Review - Regulation of Investigatory Powers Act (RIPA)

Date of final issue: 31 October 2017

Background:

The annual audit programme for 2017/18 includes an audit of compliance with the Regulation of Investigatory Powers Act (RIPA) 2000, as amended. In liaison with the RIPA Monitoring Officer, Internal Audit has carried out an interim review of particular aspects of the regulations, specifically the controls over the use of social media for investigative and research purposes.

Access to social media sites on the internet may be required to gather information for an investigation, for research or other forms of case review or assessment. Typically, officers seek to obtain such information when following up unpaid Council Tax or business rates debts, assessing applications for Housing Benefit or social housing, seeking to confirm the identity of a resident or claimant, or trying to establish the whereabouts of a tenant. Social media sources are used are when other official information is incomplete and/or does not provide the necessary verification.

The manner in which the internet is used for these purposes will determine whether it is directed surveillance, and whether it may be deemed unlawful if not authorised and conducted in accordance with RIPA. The consequences of carrying out directed surveillance involving on-line enquiries without having obtained the correct authorisations can be serious. If surveillance is deemed unlawful this may jeopardise any attempt to bring a prosecution or take enforcement action. Also, any enquiries that breach a person's right to privacy could result in action for damages against the Council.

Main points

The extent of the official use of social media sites varies across services, and teams within services. Some teams are frequent users of social media, more often when staff members use social media themselves privately – they regard social media as an entirely normal information source to be used in their Council work. These teams are well versed in the practical methods to access such information but appear to have no appreciation of the risks and legal pitfalls.

Staff and managers who do not use social media privately tend not to be aware of its use for official purposes. Where individuals do not use social media privately there is a lack of awareness of the way to access the sites. This can mean that potentially useful sources of information are overlooked, and managers are not aware of how to provide the necessary oversight.

The site most often accessed is Facebook, but material is also obtained from sites such as Twitter, comment forums, business websites, auction and shopping websites, and local newspapers. Where social media is used for official purposes, the frequency of use is described by officers as whatever is necessary to verify the details of claims/applications or chase up outstanding payments.

Detailed records of access to social media sources are kept in a few teams in order to comply with the Criminal Procedure and Investigations Act (CPIA) - either as normal professional practice in Counter Fraud teams or when the information obtained might be required as evidence. The more common position is that no records of social media access are maintained.

The RIPA Monitoring Officer has prepared draft guidance that includes detail on the RIPA legislation, the authorisation that may be required for surveillance involving social media sites, and related issues such as the Data Protection (DPA) 1998. Internal Audit strongly supports the publication of such guidance. The draft guidance would benefit from updating to include clear references to the wide range of official uses for social media sites, together with simple practical information on how to access the sites and the controls that need to be applied in certain situations. The guidance would gain additional benefit from being supported by training that is targeted at the staff, team leaders and managers in the services that require access to social media sites in their day to day work.

The report contained one recommendation that detailed the specific issues that should be covered in the guidance and linked training.

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
HACF – Head of Audit and Counter Fraud
HB – Housing Benefit
HRA – Housing Revenue Account. Refers to Council owned housing
ISO – International Organisation for Standardisation
IT – Information Technology
JTP – Joint Transformation Project
LATC – Local Authority Trading Company
LDC – Lewes District Council
NDR – Non Domestic Rates
NFI – National Fraud Initiative
PIs – Performance Indicators
PSIAS – Public Sector Internal Audit Standards
PSAA - Public Sector Audit Appointments
QAIP – Quality Assurance and Improvement Programme
RO – Returning Officer
RTB – Right to Buy
SFIS – Single Fraud Investigation Service
WGA – Whole of Government Accounts

Agenda Item No:	**8**	**Report No:**	**168/17**
Report Title:	**Treasury Management**		
Report To:	**Audit and Standards Committee**	**Date: 27 November 2017**	
Ward(s) Affected:	**All**		
Report By:	**Alan Osborne, Deputy Chief Executive**		

Contact Officer(s)-

Name(s): **Stephen Jump**
Post Title(s): **Deputy Head of Finance, Finance Shared Service**
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Purpose of Report:

To present details of recent Treasury Management activity.

Officers Recommendation:

1. To note the Mid-year Treasury Management Report 2017/2018.

2. To confirm to Cabinet that Treasury Management activity between 1 September and 31 October 2017 has been in accordance with the approved Treasury Strategies for that period.

Reasons for Recommendations

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 Treasury Strategy Statement also requires the Audit and Standards Committee to review the Mid-year Treasury Management Report.

2 Mid-year Treasury Management Report 2017/2018

2.1 As well as reviewing details of Treasury transactions during the course of the year, the Audit and Standards Committee (and Cabinet) is also required to review a formal Mid-year summary report. Council then considers this report in accordance with best practice and guidance issued by the Chartered Institute of Public Finance and Accountancy.

2.2 The timing of the Committee/Council meeting cycle has meant that the Audit and Standards Committee does not have the opportunity to consider the Mid-year Report for 2017/2018 in advance of Cabinet, which received it on 13 November

2017 and recommended to Council that it should be approved when it meets on 6 December. However, it remains appropriate for the Audit and Standards Committee to consider this report, attached as an Appendix, with any specific comments being passed on to Council when it meets.

2.3 The Mid-year Report covers the period 1 April to 30 September 2017. It confirms that the key elements of the approved Treasury and Investment Strategy have been complied with during the first half of the year. Section 2 of the Report provides a summary of performance against the key targets in the 2017/18 Strategy. Section 3 of the Report notes the potential need to borrow up to an additional £27.19m before the end of the financial year, dependent on the delivery of a number of projects within the Council's approved capital programme, for example £20m in loan facilities to Lewes Housing Investment Company (LHIC) and Aspiration Homes. The cost to the General Fund of any new borrowing in respect of these facilities would be offset by income generated from it eg LHIC would pay interest to the Council on any loan advanced to it. The remainder of the Report gives a more explanation of borrowing and investment activity and the broader economic context within which officers have worked.

3 Treasury Management Activity

3.1 The timetable for reporting Treasury Management activity in 2017/2018 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
27 November 2017	1 September to 31 October 2017
22 January 2018	1 November to 31 December 2017
19 March 2018	1 January to 28 February 2018

3.2 Fixed Term Deposits pending maturity

The following table shows the fixed term deposits held at 31 October 2017 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.The minimum rating required for deposits made after 1 April 2017 is long term BBB+ (Fitch).

Ref	Counterparty	Date From	Date To	Days	Principal £	Int Rate %	Long-term rating
235917	Eastbourne Borough Council	29/08/17	30/11/17	93	3,000,000	0.26	*
236217	Eastbourne Borough Council	08/09/17	08/12/17	91	4,000,000	0.25	*
					7,000,000		

*UK Government body and therefore not subject to credit rating

3.3 Fixed Term Deposits which have matured in the reporting period

The table below shows the fixed term deposits which have matured since 1 September 2017, 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 £23.2m over this period.

Ref	Counterparty	Date From	Date To	Days	Principal £	Int Rate %	Long-term rating
235717	Debt Management Office	23/08/17	04/09/17	12	1,000,000	0.10	*
236017	Debt Management Office	01/09/17	04/09/17	3	5,000,000	0.10	*
236117	Debt Management Office	04/09/17	11/09/17	7	5,000,000	0.10	*
236317	Debt Management Office	11/09/17	13/09/17	2	4,500,000	0.10	*
236417	Newport City Council	02/10/17	19/10/17	17	1,200,000	0.17	*
236517	Waltham Forest LBC	02/10/17	19/10/17	17	1,000,000	0.18	*
236617	Debt Management Office	02/10/17	19/10/17	17	1,500,000	0.10	*
236717	Debt Management Office	16/10/17	19/10/17	3	4,000,000	0.10	*
	Total				23,200,000		
	*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, and made, in the period 1 September to 31 October 2017 was 0.20%. The bank Base Rate remained at 0.25% throughout the period. It was increased to 0.50% on 2 November 2017.

3.4 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 £2m generating interest of approximately £600. On 2/3 October 2017, the amount held overnight with Lloyds Bank was £3.28m, compared with the £2m limit specified in the Treasury strategy. This situation arose because an investment decision taken on 2 October did not complete as planned.

	Balance at 31 Oct '17 £'000	Average balance £'000	Current interest rate %
Santander Business Reserve Account	2,000	1,100	0.15%
Lloyds Bank Corporate Account	647	903	0.15%

3.5 Use of Money Market Funds

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

	Balance at 31 Oct '17 £'000	Average balance £'000	Average return %
Goldman Sachs Sterling Liquid Reserves Fund	Nil	2,230	0.29%
Deutsche Managed Sterling Fund	500	2,336	0.27%

3.6 Purchase of Treasury Bills (T-Bills)

The table below shows the T-Bills held at 31 October 2017 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 October 2017					
UK Treasury Bill 0%	22 Jan 18	✓	23 Oct 17	1,000	0.358
UK Treasury Bill 0%	25 Jan 18	✓	23 Oct 17	1,000	0.347
				2,000	
Matured during the period					
UK Treasury Bill 0%	25 Sep 17		29 Aug 17	1,000	0.199
UK Treasury Bill 0%	25 Sep 17		29 Aug 17	1,000	0.188
UK Treasury Bill 0%	25 Sep 17		29 Aug 17	1,000	0.177
				3,000	

3.7 Secured Investments

The investment below is 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
XS113251472	Bank of Nova Scotia	22 Jul 16	02 Nov 17	414	£2,000,000	0.53	AAA

3.8 Tradeable Investments

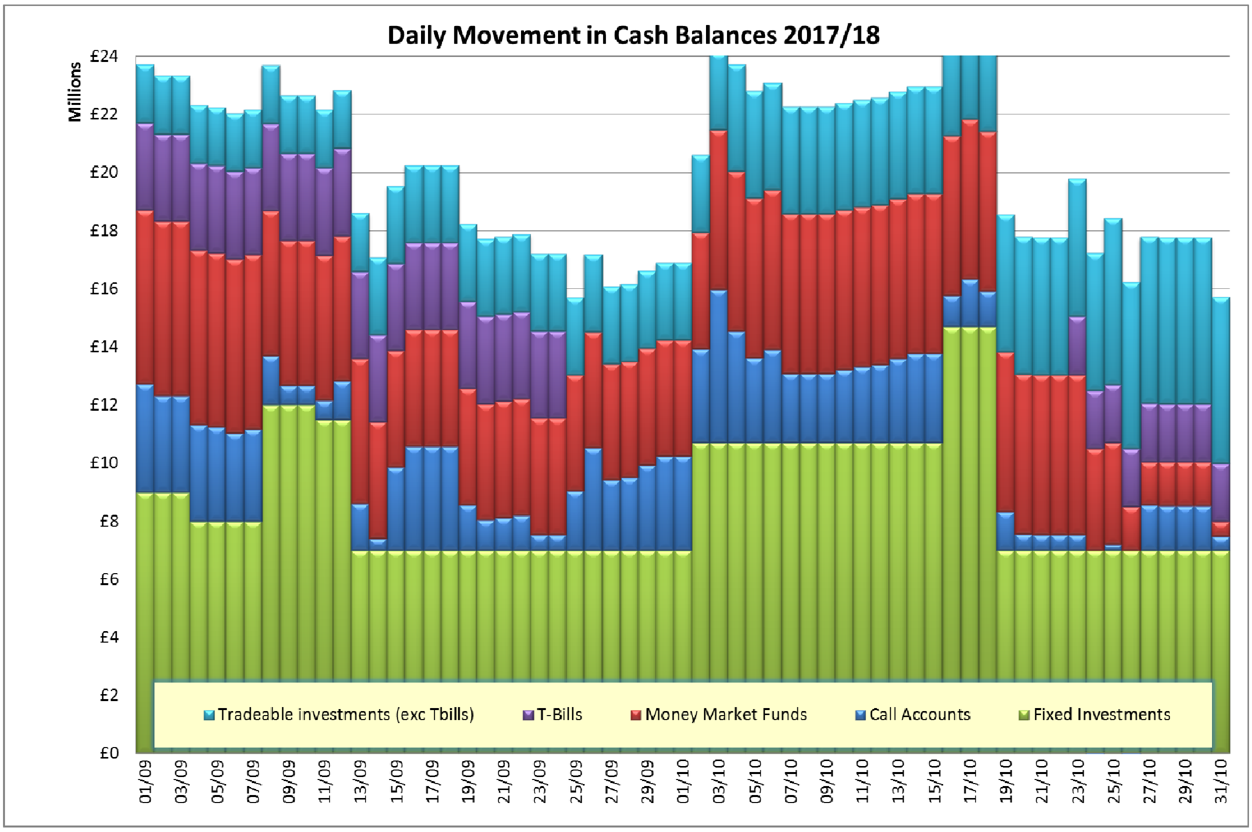
The table below shows the Tradeable Investments held at 31 October 2017.

Ref	Counterparty	Categ -ory	Date From	Date To	Days	Principal £	Rate %	Long Term Rating
Held at 31 October 2017 (all purchased in period)								
XS1015890210	Daimler AG	FB	14 Sep 17	16 Jul 18	305	650,000	0.690	A-
XS1015890210	Daimler AG	FB	04 Oct 17	16 Jul 18	285	1,000,000	0.805	A-
XS0432619913	Vodafone Group plc	FB	19 Oct 17	05 Dec 17	47	1,000,000	0.450	BBB+
GB00BDXFTR27	Nordea AB	CD	25 Oct 17	25 Apr 18	182	1,000,000	0.440	AA-
						3,650,000		

FB – Fixed Bond **CD** – Certificate of Deposit

3.9 Overall investment position

The chart below summarises the Council's investment position over the period 1 September to 31 October 2017. It shows the total sums invested each day as Fixed Term deposits, T-Bills, amounts held in Deposit accounts, MMFs and Tradeable Investments.



3.10 Borrowing

Temporary borrowings made for cash-flow management purposes during the period are shown below.

Ref	Counterparty	Date From	Date To	Days	Principal £	Cost
Borrowings at 31 October 2017						
	Total				Nil	
Borrowings made and repaid in period						
	Lloyds Bank overdrawn balance	23 Oct 17	24 Oct 17	1	1,385,913	
	Lloyds Bank overdrawn balance	25 Oct 17	26 Oct 17	1	469,572	
	Total				1,855,485	£10

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

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

Risk Management Implications

5 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

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

Legal Implications

7 None arising from this report.

Appendix

Mid-year Treasury Management Report 2017/2018

Background Papers

Treasury Strategy Statement 2017/2018

APPENDIX

Lewes District Council

Mid-year Treasury Management Report 2017/2018

Contents

1. Background

1.1 The Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management (the Code) recommends that full Council should receive every year reports on Treasury Management policies and activity before the start of the year, mid-year and after the end of the year. The intention is that those with ultimate responsibility for the Treasury Management function appreciate fully the implications of Treasury Management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

1.2 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."*

1.3 This mid-year report covers the period 1 April to 30 September 2017.

2. Overall Summary of Activity

2.1 At its meeting in February 2017, the Council agreed its Treasury Management Strategy Statement and Investment Strategy 2017/18 to 2019/20. The table below lists the key elements of that Strategy and records actual performance in the first six months of the year against each one of them.

Key Element	Target in Strategy	Actual Performance	
Borrowing			
Underlying need to borrow (CFR) at year end, 31 March 2018	£84.016 million	£107.069 million (projection 31 March)	-
Internal borrowing at year end	£27.343 million	£23.206 million with potential need to borrow additional £27.190m (projection 31 March)	-
New external long-term borrowing in year	None anticipated	None undertaken Apr to Sept '17.	✓
Debt rescheduling in year	Review options but not anticipated	Options kept under review, none undertaken Apr to Sept' 17.	✓
Interest payments on external borrowing	£1.730 million	£0.861m (to date)	✓
Investments			
Minimum counterparty credit rating for unsecured investments	Long-term BBB+ (does not apply to Government and other local authorities which have the highest ratings)	Long-term A	✓
Income returns from external investments	£0.104m	£0.043m (to date)	✓

Key Element	Target in Strategy	Actual Performance	
Appointment of Investment Consultants			
Independent Treasury Adviser to be retained	Decide on options - Arlingclose contract ends June 2017	Exercised option to extend Arlingclose contract by 12 months to June 2018	✓
Reporting and Training			
Reports to be made to Audit and Standards Committee and Cabinet	Every meeting	Every meeting	✓
Briefing sessions for Councillors and Staff	Treasury Adviser to provide	Staff training took place September 2017. Councillor briefing session anticipated December 2017/January 2018	✓

2.2 For those who are looking for more than this overall confirmation that all treasury management and investment activity in 2017/18 has been carried out in accordance with the Council's agreed Strategy, the remainder of this report analyses each of the key elements in more depth. Appendix A, supplied by Arlingclose explores the economic background to the year's activity and Appendix B lists all term deposits made in the first half of the year. A Glossary appears at the end of the document to explain the technical terms which could not be avoided when writing this report.

3. Detailed Analysis - Borrowing

3.1 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 2014/15 local authorities were able to bid for an increase in the housing debt cap in order to enable specific projects. A bid from this Council was successful and the debt cap has been increased to £75.248m to match expenditure incurred in building new houses on 7 specified former garage sites

3.2 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 2017/18.

3.3 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.

3.4 As noted above, the level of CFR increases each year by the amount of unfinanced capital expenditure and is reduced by the amount that the Council sets aside for the repayment of borrowing. The original CFR projection for 2017/18, along with an updated analysis, is shown in the table below. The increases in capital expenditure and financing shown reflect the approved capital programme as at September 2017, and assume that all projects are completed in the year. That outcome is unlikely however - the capital programme represents an allocation of funds to specific long-term projects some of which span financial years, for example the development of a new fire station on the Springman House site in the North Street quarter Lewes for which £3.5m is allocated. This project had not been included in the original capital programme for 2017/18, which has also been amended to include £20m as a loan allocation to Lewes Housing investment Company and Aspiration Homes (a Limited Liability Partnership co-owned by the Council and Eastbourne Borough Council) to facilitate the development of new mixed tenure housing.

	2017/18 Original £m	2017/18 Projected £m
Opening CFR	79.580	77.042
Capital expenditure in year (projected)	14.556	47.587
Less financed	(8.893)	(16.450)
Less amount set aside for debt repayment	(1.137)	(1.114)
Closing CFR	84.016	107.069

3.5 As at 30 September 2017, capital expenditure with a total value of £2.706m had been incurred (excluding commitments) compared with the approved capital programme of £47.6m (including £6.3m brought forward from 2016/17). £16.5m of total capital expenditure will be funded from existing capital resources, with £31.1m to be funded from borrowing, including £20.0m for the loan facility to Lewes Housing Investment Company and Aspiration Homes, £4.9m to continue a programme of commercial development, £3.5m for the Springman House site and £2.7m for new Council-owned homes.

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

	2017/18 Original £m	2017/18 Projected £m
General Fund CFR	18.848	39.823
Housing Revenue Account CFR	65.168	67.246
Total CFR	84.016	107.069

3.7 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). It indicates a potential need to borrow an additional £27.190m dependent on the delivery of the capital programme projects noted in para 3.5 and the level of working capital held. Any need to borrow can be met either by long-term fixed rates loans (the Council qualifies for new borrowing at the 'Certainty Rate', 0.20% below the PWLB standard rate) or short-term borrowing (which is likely to be avaiable at lower rates of interest than long-term loans), or a combination. Officers will liaise closely with Arlingclose when deciding the duration or terms of any new borrowing. The cost to the General Fund of any new borrowing would be offset by income generated from the project (eg Lewes Housing Investment Company would pay interest to the Council on all loans advanced to it).

	31/3/18 Original £m	31/3/18 Projected £m
(a) Capital Financing Requirement	84.016	107.069
(b) Actual external borrowing	(56.673)	(56.673)
(c) Use of Balances and Reserves and working capital as alternative to borrowing (a)–(b)	(27.343)	(23.206)
(d) Potential additional borrowing requirement	0.000	27.190

3.8 Total interest payable on long-term borrowing in the period to 30 September 2017 was £0.861m, representing the first of two instalments of interest due on a £5m market loan from Barclays Bank at the rate of 4.5% with a term of 50 years maturing in April 2054 and a £51.67m portfolio of loans from the PWLB. The PWLB loan portfolio comprises £46.67m spread across 11 separate loans with a range of fixed interest rates and maturity dates and a £5m variable rate loan currently charged at 0.45%.

3.9 Through the year, officers, supported by Arlingclose, monitor opportunities for the rescheduling of external loans and the possibility of repayment utilising cash balances that would otherwise be invested. No rescheduling opportunities arose during the first half of 2017/18 which would be cost-effective for the General Fund and Housing Revenue Account in the light of current and expected market conditions.

3.10 In the period to September 2017, four temporary loans had been taken for cash flow purposes. The highest level of temporary borrowing was £7.0m (27 April 2017) and all loans had been repaid by 1 June 2017.

4. Detailed Analysis - Investments

4.1 The Council held on average £16.11m available for investment in the period to 30 September 2017. This comprised working cash balances, capital receipts, earmarked reserves and developer contributions held pending use.

4.2 The Council's general policy objective is to invest its surplus funds prudently. The Council's investment priorities have continued to be:

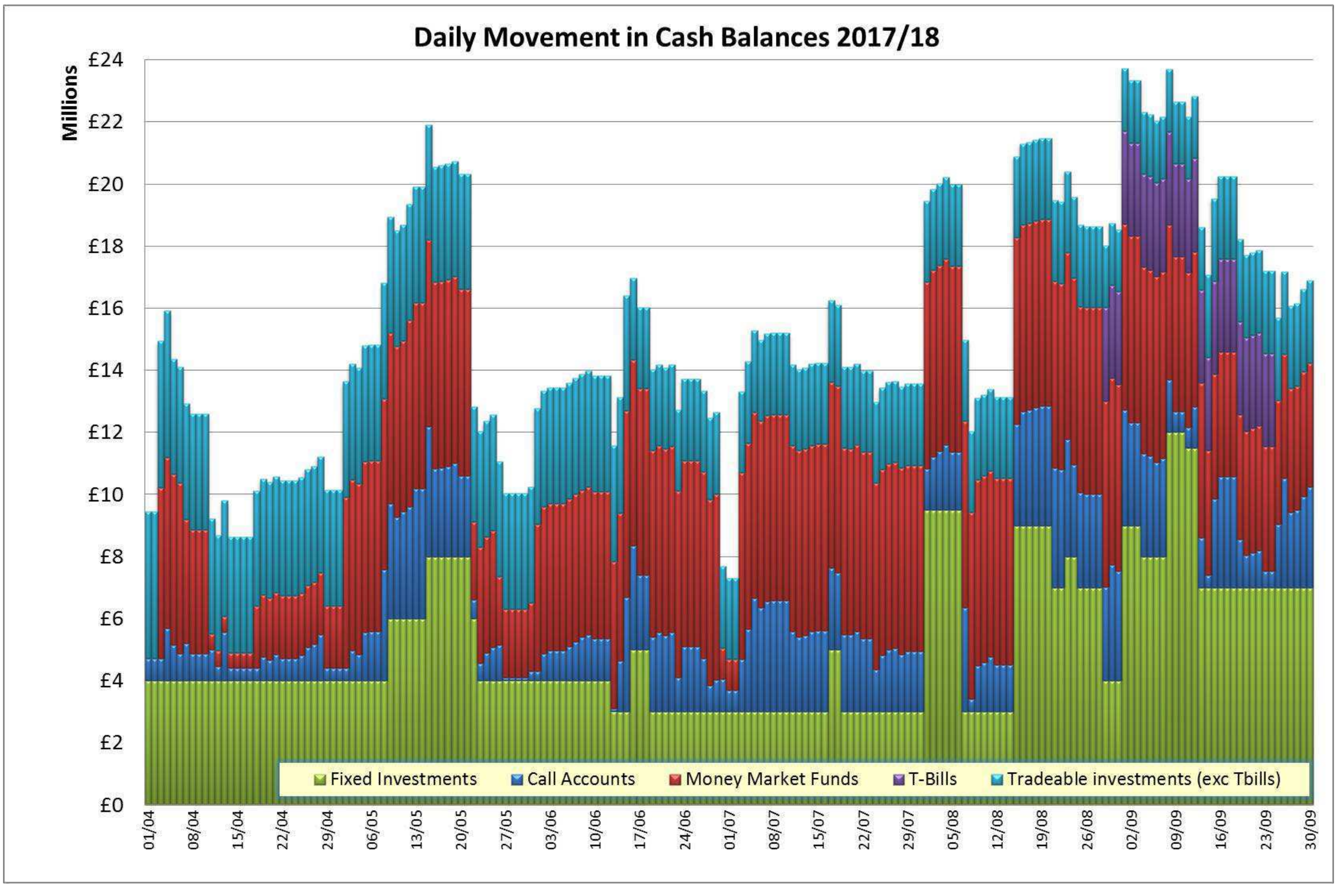
highest priority - security of the invested capital;
followed by - liquidity of the invested capital;
finally - an optimum yield commensurate with security and liquidity.

4.3 All of the Council's investments have been managed in-house. Security of capital has been maintained by following the counterparty policy set out in the Investment Strategy for 2017/2018. Investments during the period included:

- Fixed Term Deposits with the Debt Management Office (total £36.50m)

- Fixed Term Deposits with other Local Authorities (total £15.20m)
- Fixed Term Deposits with UK Banks/Building Societies (total £5.00m)
- Investments in Money Market Funds (MMFs) (average balance held in period £4.85m)
- United Kingdom Treasury Bills (average balance £0.38m)
- Tradable Investments -Floating Rate Notes, Certificates of Deposit, Bonds (average balance £3.13m)
- Deposit accounts with UK Banks (average balance held in year £1.13m)
- Overnight deposits with the Council's banker, Lloyds Bank (average balance held in year £0.89m)

The chart below shows the profile of total investments from 1 April to 30 September. The total invested ranged from £7.3m (end of June) to £23.3m (beginning of September).



4.4 The Council has approved the use of two MMFs, Deutsche Bank – Deutsche Global Liquidity Series and Goldman Sachs Asset Management International.

4.5 Counterparty credit quality was assessed and monitored with reference to credit ratings (a minimum long-term counterparty rating of BBB+ across all three rating agencies Fitch, Standard and Poors, and Moody's applied); credit default swaps; GDP of the country in which the institution operates; the country's net debt as a percentage of GDP; any potential support mechanisms and share price.

4.6 In keeping with Government guidance on investments, the Council maintained a sufficient level of liquidity through the use of MMFs, overnight deposits and deposit accounts.

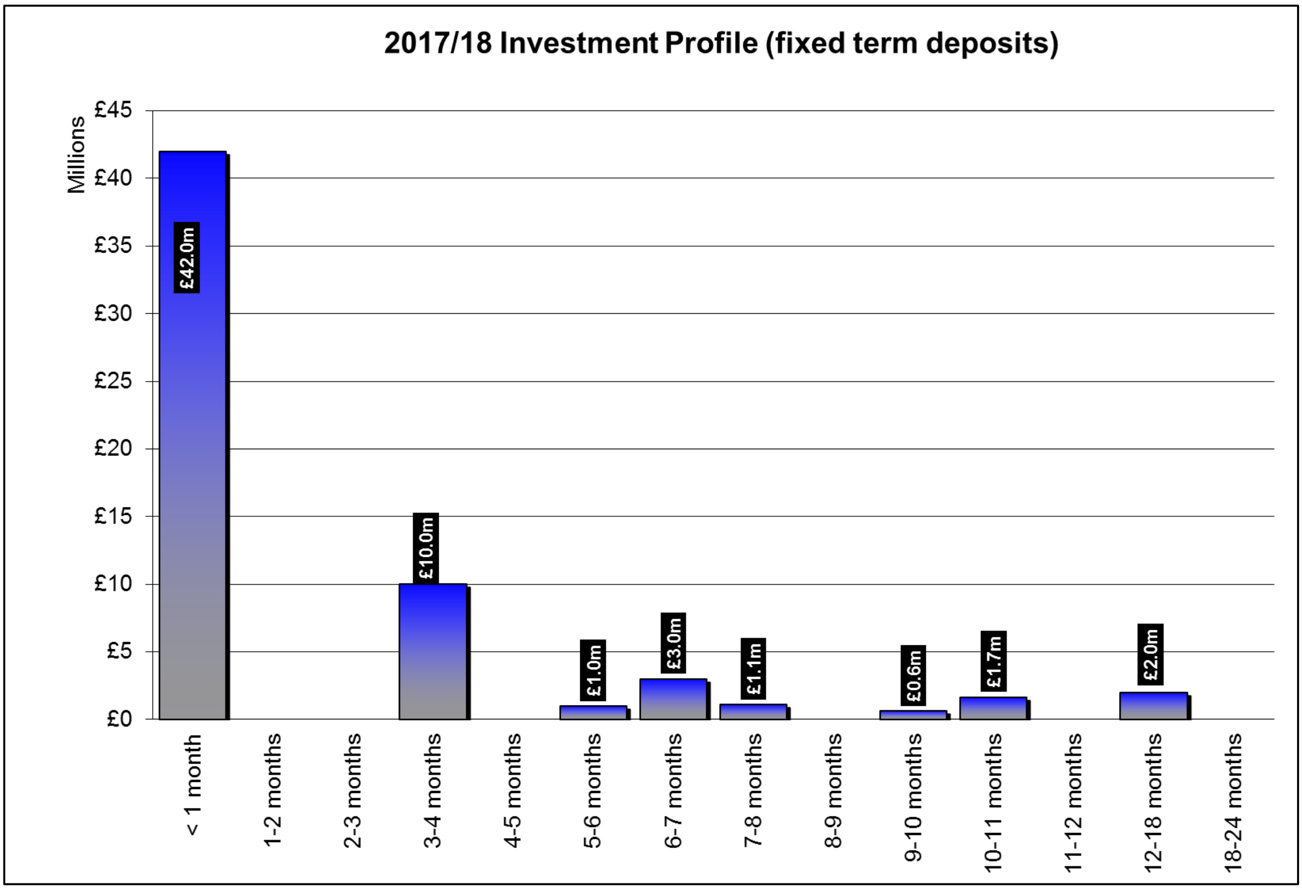
4.7 The Council sought to optimise returns commensurate with its objectives of security and liquidity. The Treasury Management Strategy anticipated no change to the UK Bank Rate of 0.25% through the whole of 2017/18. Although the Bank of England has made no change during the first half of the year, minutes of the September 2017 meeting of its Monetary Policy Committee implied an increase in Bank Rate in coming months with the aim of returning inflation to target. While Arlingclose's central view remains that the Bank Rate will remain unchanged through to December 2020, they have noted a risk of an increase to 0.50% in September 2018.

4.8 Interest generated from investments in the year to date was £0.043m) and is projected to attain the full year budget, £0.104m.

4.9 The average rate of return from investments at the end of Quarter 1 and Quarter 2 is shown in the table below, along with comparative benchmark information.

	Lewes District Council	7 Day Libid
Average rate of investments in Q1 end 30 June 2017	0.44%	0.11%
Average rate of investments in Q2 end 30 Sept 2017	0.41%	0.11%
Average rate of return Q1 to Q2	0.43%	0.11%

4.10 A full list of temporary deposits and fixed maturity date investments made in the year is given at Appendix B. All investments were made with UK institutions, and no new deposits were made for periods in excess of one year. The chart below gives an analysis of fixed term deposits by duration.



5. Counterparty Update

5.1 There were a few credit rating changes during the quarter. The significant change was the downgrade by Moody's to the UK sovereign rating in September from Aa1 to Aa2 which resulted in subsequent downgrades to sub-sovereign entities including local authorities. Moody's downgraded Standard Chartered Bank's long-term rating to A1 from Aa3 on the expectation that the bank's profitability will be lower following management's efforts to de-risk their balance sheet. The agency also affirmed Royal Bank of Scotland's and NatWest's long-term ratings at Baa1, placed Lloyds Bank's A1 rating on review for upgrade, revised the outlook of Santander UK plc, and Nationwide and Coventry building societies from negative to stable but downgraded the long-term rating of Leeds BS from A2 to A3. The agency downgraded long-term ratings of the major Canadian banks on the expectation of a more challenging operating environment and the ratings of the large Australian banks on its view of the rising risks from their exposure to the Australian housing market and the elevated proportion of lending to residential property investors.

5.2 S&P also revised Nordea Bank's outlook to stable from negative, whilst affirming their long-term rating at AA-. The agency also upgraded the long-term rating of ING Bank from A to A+.

5.3 Ring-fencing, which requires the larger UK banks to separate their core retail banking activity from the rest of their business, is expected to be implemented within the next year. In May, following Arlingclose's advice, the Council reduced the maximum duration of potential unsecured investments with Bank of Scotland, HSBC Bank and

Lloyds Bank from 13 months to 6 months as until banks' new structures are finally determined and published, the different credit risks of the 'retail' and 'investment' banks cannot be known for certain.

5.4 New EU regulations for Money Market Funds were finally approved and published in July and existing funds will have to be compliant by no later than 21st January 2019. The key features include Low Volatility NAV (LVNAV) Money Market Funds which will be permitted to maintain a constant dealing NAV, providing they meet strict new criteria and minimum liquidity requirements. MMFs will not be prohibited from having an external fund rating (as had been suggested in draft regulations). Arlingclose expects most of the short-term MMFs it recommends to convert to the LVNAV structure and awaits confirmation from each fund.

5.5 At 30 September 2017, the following UK institutions met the Council's investment criteria and were potential counterparties:

Bank of Scotland plc	Barclays Bank plc
Close Brothers Ltd	Goldman Sachs International Bank
HSBC Bank plc	Lloyds Bank plc
Santander UK plc	Standard Chartered Bank
Coventry Building Society	Leeds Building Society
Nationwide Building Society	

A number of other institutions also met the criteria, although there is very limited opportunity to place deposits with them.

6. Internal Borrowing

6.1 Since 1 April 2012 the Council has adopted a 'two pool' approach to the accounting treatment of loans. Under this approach, interest on any external borrowing in respect of expenditure on General Fund services is to be charged to the General Fund, and interest on any external borrowing in respect of the Council's housing stock (Housing Revenue Account (HRA)) is to be charged to the HRA. At the start of 2017/2018, all external borrowing was attributed to the HRA.

6.2 Where the HRA or General Fund has surplus cash balances which allow either account to have external borrowing below its level of CFR (internal borrowing), the approved Treasury Strategy explains that the rate charged on this internal borrowing will be based on the rate of interest applicable to a one-year maturity loan from the PWLB at the start of the financial year.

6.3 It is expected that an interest payment will be made from the HRA to the General Fund in 2017/18, but the final amount will not be determined until the close of the year, dependent on the capital programme outturn. The HRA capital programme at 30 September 2017 includes £2.72m in respect of the construction or acquisition of new properties, to be part-funded by borrowing but it is not expected to take new loans from the PWLB or other source. This constitutes internal borrowing by the HRA from the General Fund and an interest charge will be made as outlined above.

7. Compliance with Prudential Indicators

The Council can confirm that it is on track to comply with its Prudential Indicators for 2017/18, which were set in February 2017 as part of the Council's Treasury Management Strategy Statement. Actual borrowing has remained within the Authorised Limit for External Debt (£85.5m) and the Operational Boundary for External Debt (£80.0m).

8. Regulatory Updates

8.1 **MiFID II.** Local authorities are currently treated by regulated financial services firms as professional clients who can "opt down" to be treated as retail clients instead. However, from 3 January 2018, as a result of the EU's second Markets in Financial Instruments Directive (MiFID II), local authorities will be treated as retail clients who can "opt up" to be professional clients, providing that they meet certain criteria. Regulated financial services firms include banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments. In order to opt up to professional, the local authority must have an investment balance of at least £10m and the person authorised to make investment decisions on behalf of the authority must have at least one year's relevant professional experience. In addition, the regulated firm must assess that that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved.

8.2 The main additional protection for retail clients is a duty on the regulated firm to ensure that the investment is "suitable" for the client. However, local authorities are not protected by the Financial Services Compensation Scheme nor are they eligible to complain to the Financial Ombudsman Service whether they are retail or professional clients. It is also likely that retail clients will face an increased cost and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice.

8.3 The Council meets the conditions to opt up to professional status and intends to do so in order to maintain its current MiFID status, retaining access to a wider range of investment categories, brokers and treasury advisors than would be available to it as a retail client.

8.4 **CIPFA Consultation on Prudential and Treasury Management Codes:** In February 2017 CIPFA canvassed views on the relevance, adoption and practical application of the Treasury Management and Prudential Codes and after reviewing responses launched a further consultation on changes to the codes in August with a deadline for responses of 30th September 2017.

8.5 The proposed changes to the Prudential Code include the production of a new high-level Capital Strategy report to full Council which will cover the basics of the capital programme and treasury management. The prudential indicators for capital expenditure and the authorised borrowing limit would be included in this report but other indicators may be delegated to another committee. There are plans to drop certain prudential indicators, however local indicators are recommended for ring fenced funds (including the HRA) and for group accounts (incorporating Lewes

Housing Investment Company). Other proposed changes include applying the principles of the Code to subsidiaries.

8.6 Proposed changes to the Treasury Management Code include the potential for non-treasury investments such as commercial investments in properties in the definition of "investments" as well as loans made or shares brought for service purposes. Another proposed change is the inclusion of financial guarantees as instruments requiring risk management and addressed within the Treasury Management Strategy. Approval of the technical detail of the Treasury Management Strategy may be delegated to a committee rather than needing approval of full Council. There are also plans to drop or alter some of the current treasury management indicators.

8.7 CIPFA intends to publish the two revised Codes towards the end of 2017 for implementation in 2018/19, although CIPFA plans to put transitional arrangements in place for reports that are required to be approved before the start of the 2018/19 financial year. The Department of Communities and Local Government (DCLG) and CIPFA wish to have a more rigorous framework in place for the treatment of commercial investments as soon as is practical. It is understood that DCLG will be revising its Investment Guidance (and its MRP guidance) for local authorities in England; however there have been no discussions with the devolved administrations yet.

9. Reporting and Training

9.1 The Deputy Chief Executive has reported the details of treasury management activity to each meeting of the Audit and Standards Committee and Cabinet held to date in 2017/18.

9.2 All councillors tasked with treasury management responsibilities, including scrutiny of the treasury management function, are expected to be offered the opportunity to attend a local briefing session led by Arlingclose in December 2017 or January 2018.

9.3 The training needs of the Council's treasury management staff continue to be reviewed as part of the annual corporate staff appraisal/training needs assessment process for all Council employees. Staff continue to attend Arlingclose workshops, when appropriate to their needs, alongside colleagues from other local authorities during 2017/18.

10. Investment Consultants

10.1 The Council appointed Arlingclose as its Treasury Adviser in 2012 following an open procurement. The agreement with Arlingclose was for an initial four-year term expiring on 30 June 2016, with the Council having the option to extend for a further year.

10.2 The Council exercised the option to extend this agreement to the end of June 2017 and following discussion with Arlingclose has now opted to maintain the appointment for a further year. The appointment of an investment consultant from July 2018 onwards is expected to be made in conjunction with Eastbourne Borough Council given that a shared finance team (with treasury management responsibility) is being established.

Appendix A – Economic Background explained by Arlingclose

The UK Consumer Price Inflation (CPI) index rose with the data print for August showing CPI at 2.9%, its highest since June 2013 as the fall in the value of sterling following the June 2016 referendum result continued to feed through into higher import prices. The new inflation measure CPIH, which includes owner occupiers' housing costs, was at 2.7%.

The unemployment rate fell to 4.3%, its lowest since May 1975, but the squeeze on consumers intensified as average earnings grew at 2.5%, below the rate of inflation. Economic activity expanded at a much slower pace as evidenced by Q1 and Q2 GDP growth of 0.2% and 0.3% respectively. With the dominant services sector accounting for 79% of GDP, the strength of consumer spending remains vital to growth, but with household savings falling and real wage growth negative, there are concerns that these will be a constraint on economic activity in the second half of calendar 2017.

The Bank of England made no change to monetary policy at its meetings in the first half of the financial year. The vote to keep Bank Rate at 0.25% narrowed to 5-3 in June highlighting that some MPC members were more concerned about rising inflation than the risks to growth. Although at September's meeting the Committee voted 7-2 in favour of keeping Bank Rate unchanged, the MPC changed their rhetoric, implying a rise in Bank Rate in "the coming months". Arlingclose is not convinced the UK's economic outlook justifies such a move at this stage, but the Bank's interpretation of the data seems to have shifted.

Geopolitical tensions escalated in August as the US and North Korea exchanged escalating verbal threats over reports about enhancements in North Korea's missile programme. The provocation from both sides helped wipe off nearly $1 trillion from global equity markets but benefited safe-haven assets such as gold, the US dollar and the Japanese yen. Tensions remained high, with North Korea's threat to fire missiles towards the US naval base in Guam, its recent missile tests over Japan and a further testing of its latent nuclear capabilities.

Prime Minister Theresa May called an unscheduled General Election in June, to resolve uncertainty but the surprise result has led to a minority Conservative government in coalition with the Democratic Unionist Party. This clearly results in an enhanced level of political uncertainty. Although the potential for a so-called hard Brexit is diminished, lack of clarity over future trading partnerships, in particular future customs agreements with the rest of the EU block, is denting business sentiment and investment. The reaction from the markets on the UK election's outcome was fairly muted, business confidence now hinges on the progress (or not) on Brexit negotiations, the ultimate 'divorce bill' for the exit and whether new trade treaties and customs arrangements are successfully concluded to the UK's benefit.

In the face of a struggling economy and Brexit-related uncertainty, Arlingclose expects the Bank of England to take only a very measured approach to any monetary policy tightening, any increase will be gradual and limited as the interest rate backdrop will have to provide substantial support to the UK economy through the Brexit transition.

Outlook for the remainder of 2017/18

The UK economy faces a challenging outlook as the minority government continues to negotiate the country's exit from the European Union. Both consumer and business confidence remain subdued. Household consumption growth, the driver of UK GDP growth, has softened following a contraction in real wages. Savings rates are at an all-time low and real earnings growth (i.e after inflation) struggles in the face of higher inflation.

The Bank of England's Monetary Policy Committee has changed its rhetoric, implying a rise in Bank Rate in "the coming months". Arlingclose is not convinced the UK's economic outlook justifies such a move at this stage, but the Bank's interpretation of the data seems to have shifted.

This decision is still very data dependant and Arlingclose is, for now, maintaining its central case for Bank Rate at 0.25% whilst introducing near-term upside risks to the forecast as shown below. Arlingclose's central case is for gilt yields to remain broadly stable in the across the medium term, but there may be near term volatility due to shifts in interest rate expectations.

	Dec-17	Mar-18	Jun-18	Sep-18	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20
Official Bank Rate													
Upside risk	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50	0.50
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**
Downside risk	0.00	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25

Appendix B – Term deposits made and/or maturing April to September 2017

Ref	Counterparty	From	To	Da	Principal	Int	Rating
232016	Thurrock Borough Council	28 Nov 16	30 May 17	183	3,000,000	0.35%	*
233516	Nationwide Building Society	13 Dec 16	13 Jun 17	182	1,000,000	0.42%	A+
234917	Coventry Building Society	9 May 17	23 May 17	14	2,000,000	0.13%	A
235017	Eastbourne Borough Council	30 May 17	30 Aug 17	92	3,000,000	0.32%	*
235117	Debt Management Office	15 May 17	22 May 17	7	2,000,000	0.10%	*
235217	Coventry Building Society	16 Jun 17	19 Jun 17	3	2,000,000	0.11%	A
235317	Debt Management Office	17 Jul 17	19 Jul 17	2	2,000,000	0.10%	*
235417	Debt Management Office	1 Aug 17	7 Aug 17	6	6,500,000	0.10%	*
235517	Debt Management Office	15 Aug 17	21 Aug 17	6	2,000,000	0.10%	*
235617	Debt Management Office	15 Aug 17	25 Aug 17	10	4,000,000	0.10%	*
235717	Debt Management Office	23 Aug 17	4 Sep 17	12	1,000,000	0.10%	*
235817	Debt Management Office	25 Aug 17	29 Aug 17	4	3,000,000	0.10%	*
235917	Eastbourne Borough Council	29 Aug 17	30 Nov 17	93	3,000,000	0.26%	*
236017	Debt Management Office	1 Sep 17	4 Sep 17	3	5,000,000	0.10%	*
236117	Debt Management Office	4 Sep 17	11 Sep 17	7	5,000,000	0.10%	*
236217	Eastbourne Borough Council	8 Sep 17	8 Dec 17	91	4,000,000	0.25%	*
236317	Debt Management Office	11 Sep 17	13 Sep 17	2	4,500,000	0.10%	*

Glossary of 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 other 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, multilateral development banks and corporates. 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 financed 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 are 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.

LEWES DISTRICT COUNCIL

ANNUAL AUDIT LETTER

Audit for the year ended 31 March 2017

EXECUTIVE SUMMARY

Purpose of the letter

This Annual Audit Letter summarises the key issues arising from the work that we have carried out in respect of the financial year ended 31 March 2017. It is addressed to the Council but is also intended to communicate the key findings we have identified to key external stakeholders and members of the public. It will be published on the website of Public Sector Audit Appointments Limited.

Responsibilities of auditors and the Council

It is the responsibility of the Council to ensure that proper arrangements are in place for the conduct of its business and that public money is safeguarded and properly accounted for.

Our responsibility is to plan and carry out an audit that meets the requirements of the National Audit Office's Code of Audit Practice (the Code), and to review and report on:

- the Council's financial statements
- whether the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

We are also required to report where we have exercised our statutory powers under the Local Audit and Accountability Act 2014 in any matter, and on our grant claims and returns certification work.

We recognise the value of your co-operation and support and would like to take this opportunity to express our appreciation for the assistance and co-operation provided during the audit.

Audit conclusions

FINANCIAL STATEMENTS

We issued an unmodified true and fair opinion on the financial statements on 29 September 2017.

We reported our detailed findings to the Audit and Standards Committee on 25 September 2017. We reported on uncorrected misstatements which management and the Audit and Standards Committee concluded were immaterial.

We identified no significant deficiencies in internal controls.

USE OF RESOURCES

We issued an unmodified conclusion on the Council's arrangements for securing economy, efficiency and effectiveness in its use of resources on 29 September 2017.

While there is a recognised funding gap in the Medium Term Financial Strategy (MTFS), we are satisfied that the Council has appropriate arrangements to continue to remain financially sustainable over the period of the MTFS. All of the required savings for 2017/18 have been identified.

The Council has made progress against all the recommendations that we raised in respect of the New Homes project in the prior year, and there is evidence that the learning from this project has been applied to other capital projects.

EXERCISE OF STATUTORY POWERS

We have not exercised our statutory powers and have no matters to report.

GRANT CLAIMS AND RETURNS CERTIFICATION

Our review of grant claims and returns for the year ended 31 March 2017 is in progress and the results will be reported upon completion of this work.

FINANCIAL STATEMENTS

OPINION	We issued an unmodified true and fair opinion on the financial statements on 29 September 2017.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that they are free from material misstatement, whether caused by fraud or error.

This includes an assessment of whether the accounting policies are appropriate to the Council's circumstances and have been consistently applied and adequately disclosed, the reasonableness of significant accounting estimates, and the overall presentation of the financial statements.

Our assessment of risks of material misstatement

Our audit was scoped by obtaining an understanding of the Council and its environment, including the system of internal control, and assessing the risks of material misstatement in the financial statements.

We set out below the risks that had the greatest effect on our audit strategy, the allocation of resources in the audit, and direction of the efforts of the audit team.

MANAGEMENT OVERRIDE OF CONTROLS	RESPONSE	FINDINGS
The primary responsibility for the detection of fraud rests with management. Their role in the detection of fraud is an extension of their role in preventing fraudulent activity. They are responsible for establishing a sound system of internal control designed to support the achievement of departmental policies, aims and objectives and to manage the risks facing the organisation; this includes the risk of fraud. Under auditing Standards there is a presumed significant risk of management override of the system of internal controls.	We reviewed the appropriateness of journal entries and other adjustments made in the preparation of the financial statements and obtained an understanding of any significant or unusual transactions. We reviewed accounting estimates for biases and evaluated whether the circumstances producing the bias, if any, represented a risk of material misstatements due to fraud.	No issues were identified in our review of the appropriateness of journal entries and other adjustments to the financial statements. We did not identify any unusual transactions. Our views on significant management estimates are reported below. Our work on accounting estimates did not identify any evidence of management bias.

REVENUE RECOGNITION	RESPONSE	FINDINGS
Under auditing Standards there is a presumption that income recognition presents a fraud risk. Our Audit Planning Report identified a risk in relation to the existence and completeness of fees and charges recorded in the Comprehensive Income and Expenditure Statement (CIES).	We tested an increased sample of fees and charges to underlying documentation, to cover the existence and accuracy of transactions throughout the year. We also tested an increased sample of receipts either side of year end, to confirm that income had been recorded in the correct period and that all income that should have been recorded at year end had been.	Our testing of revenue from fees and charges throughout the year and receipts either side of year end did not identify any issues.

FINANCIAL STATEMENTS
Continued

CHANGES IN THE PRESENTATION OF THE ACCOUNTS	RESPONSE	FINDINGS
The Code of Practice on Local Authority Accounting required a change to the presentation of some areas of the financial statements in 2016/17. This included changes to the format of the CIES , Movement in Reserves Statement and Segmental Reporting note and a new Expenditure and Funding Analysis note and Expenditure and Income analysis note. These changes required a restatement of the comparative figures. Our Audit Planning report identified a risk that these presentational changes may not have been correctly applied in the financial statements.	We checked that the required presentational changes were correctly reflected within the financial statements.	Our audit found that the financial statements largely complied with the new requirements. A few issues were identified by our audit, which were corrected in the final financial statements. These included: • Differences between the Expenditure and Funding Analysis and the outturn information in the Narrative Report • £1.5 million of housing benefit overpayment recoveries recorded as negative expenditure rather than income. • The amount disclosed for capital charges was understated, and other service expenses overstated, by £1.69 million.

RECHARGES	RESPONSE	FINDINGS
The Council is currently in the process of undergoing a major Joint Transformation Programme (JTP) with Eastbourne Borough Council to merge frontline services and back office functions. In February 2017, the vast majority of Lewes District Council employees were transferred to the employment of Eastbourne Borough Council. Recharging arrangements are in place for the employment costs of the transferred employees and for each of five service areas (Corporate Management Team, Legal Services, Information Technology, Human Resources and Asset Management). On a monthly basis Eastbourne Borough Council calculates, based on these arrangements, the amount to be recharged via invoice back to the Council. Our Audit Planning Report identified risks in respect of the completeness and accuracy of the payroll information transferred from the Lewes payroll system onto the Eastbourne payroll system, the recharges between the councils and accounting for the recharges in the CIES and senior officer remuneration disclosures.	We reviewed the work performed by Eastbourne Borough Council's payroll team in checking the migration of data from the Lewes to Eastbourne payroll systems. We reviewed the reasonableness and accuracy of the recharge arrangements in place between the councils and the manual adjustments made to record shared employee and other costs on a net accounting basis. We also reviewed the senior officers' remuneration note to check that the disclosures for senior managers and employees earning over £50,000 were complete and accurate and that the Council's share of the costs were in line with the relevant recharge arrangement.	Our review of the data migration work completed by Eastbourne Borough Council's payroll team did not identify any issues. For the five service lines which are operating full shared service arrangements under phase one of the JTP, there are set percentages in place for the amounts to be recharged, which are between 40% and 50% per service. Our checks on the amounts recharged did not identify any issues. We are satisfied that the governance structures in relation to the recharging arrangements are appropriate. We were also satisfied that the senior officers' remuneration note complied with the requirements of the Code of Practice on Local Authority Accounting , and further explanations were added to the note in the final financial statements to clarify what was included in some of the disclosures.

FINANCIAL STATEMENTS
Continued

VALUATION OF LAND AND BUILDINGS	RESPONSE	FINDINGS
Local authorities are required to ensure that the carrying value of non-current assets is not materially different to the current value (operational assets) or fair value (surplus assets, assets held for sale and investment properties) at the balance sheet date. The Council appointed an external valuer to carry out a year-end desktop review of its council dwellings, garages, surplus assets and investment properties at 31 March 2017. Due to the significant value of the Council's non-current assets, and the high degree of estimation uncertainty, we identified a risk over the valuation of non-current assets where valuations are based on assumptions or where updated valuations have not been provided for a class of assets at the year-end.	We reviewed the instructions provided to the valuer and the valuer's skills and expertise to determine if we could rely on the management expert. We checked that the basis of valuation for assets was appropriate, including whether investment properties and surplus assets were valued based on 'highest and best use.' We reviewed valuation movements against independent data showing indices of price movements for similar classes of assets. We followed up valuation movements that appeared unusual against indices, or any assets which may have had material movements since the last valuation.	We were satisfied that we could rely on the valuer and the basis of valuations applied was appropriate. **Council dwellings** Council dwellings increased by £14.8 million as a result of the valuation. This was due to a decrease in the national social housing discount factor and a 2.98% increase on the vacant possession value. This was reasonable in comparison to trends in property prices in the South East which indicated an increase of 3.8%. **Other land and buildings** Garages increased in value by 4% as a result of the valuation. This was considered reasonable in comparison to the 3.8% increase in regional property prices. The Council holds £34.1 million of other land and buildings which have not been revalued since 1 April 2014. The valuer provided material movements reports each year since the valuation, however no indexation was accounted for in these intervening years as it was not considered to be material. This approach resulted in an understatement of £1.2 million in the year end balance for specialised assets valued on a depreciated replacement cost basis. We reported this difference as an uncorrected misstatement. We were satisfied that the absence of indexation on other land and buildings valued on an existing use basis was not unreasonable, mainly because land factor indices have not changed since 2014 and the market data for investment Property Databank capital values also supports minimal change over the period. **Investment properties** All properties were revalued and an overall fair value gain of 1.5% was recognised, which compared to a 1.83% increase in national indices for IPD rental values. **Heritage assets** The Council has not applied any indexation since the valuation on 1 April 2014. Applying information from the valuer indicates that heritage assets were understated by £166,000. We reported this as an uncorrected misstatement.

FINANCIAL STATEMENTS
Continued

PENSION LIABILITIY	RESPONSE	FINDINGS
The net pension liability comprises the Council's share of the market value of assets held in the East Sussex County Council's Pension Fund and the estimated future liability to pay pensions. An actuarial estimate of the pension fund liability is calculated by an independent firm of actuaries with specialist knowledge and experience. The estimate is based on the most up to date membership data held by the pension fund and has regard to local factors such as mortality rates and expected pay rises along with other assumptions around inflation when calculating the liability. Our Audit Planning Report identified a risk that the valuation may not have been based on accurate membership data or may have used inappropriate assumptions to value the liability.	We agreed the disclosures to the information provided by the pension fund actuary. We used a PwC consulting actuary report to review the reasonableness of the assumptions used in the calculation against other local government actuaries and other observable data and to review of the actuary's methodology. We obtained assurance from the auditor of the pension fund over the controls for providing accurate membership data to the actuary. We checked whether any significant changes in membership data were communicated to the actuary.	Our review of the pensions note in the draft financial statements provided for audit noted that there had been a significant movement from investments with quoted prices not in active markets ('level 2' in the fair value hierarchy) to investments with quoted prices in active markets ('level 1' in the fair value hierarchy) compared to the prior year. Further to our enquiries, management queried the classification with East Sussex County Council, the pension fund administrators. This resulted in the actuary issuing revised reports which reclassified investment funds and unit trust equities and bonds from level 1 to level 2. This was then corrected in the final financial statements. We did not identify any other issues regarding the accuracy of the disclosures in the financial statements or the accuracy and completeness of data provided by the pension fund to the actuary. We were satisfied that the actuary adequately took account of the transfer of the majority of the Council's staff to Eastbourne Borough Council in valuing the Council's pensions liability at year end.

FINANCIAL STATEMENTS
Continued

Our application of materiality

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

We consider materiality to be the magnitude by which misstatements, including omissions, could influence the economic decisions of reasonably knowledgeable users that are taken on the basis of the financial statements.

Importantly, misstatements below these levels will not necessarily be evaluated as immaterial as we also take account of the nature of identified misstatements, and the particular circumstances of their occurrence, when evaluating their effect on the financial statements as a whole.

The materiality for the financial statements as a whole was set at £1.6 million. This was determined with reference to a benchmark of gross expenditure (of which it represents two per cent) which we consider to be one of the principal considerations for the Council in assessing the financial performance.

We agreed with the Audit and Standards Committee that we would report all individual audit differences in excess of £32,000.

Audit differences

There were no differences that were corrected in the financial statements that affected the reported surplus for the year, although a number of amendments to classifications and disclosures were made in the final financial statements. Of these, the items considered material were as follows:

- £45.6 million reclassification of pension scheme assets from those with quoted prices in active markets to those with quoted prices not in active
- £4.035 million overstatement of disclosed capital commitments at 31 March 2017
- £4 million short term loans omitted from the financial instruments note
- £1.69 million misclassification in the Expenditure and income analysed by nature disclosure.

Our audit also found four audit differences not corrected in the final financial statements:

- £1.246 million estimated understatement in the value of specialised land and buildings at 31 March 2017, as movements in values advised by the Council's valuer had not been applied since the assets were last revalued at 1 April 2014
- £166,000 estimated understatement in the value of heritage assets at 31 March 2017, as the movement in the value of Newhaven Fort advised by the Council's valuer had not been applied since the asset was last revalued at 1 April 2014
- Overstatement of expenditure of £74,000, due to understatement of expenditure in the prior year
- £130,000 overstatement of the revaluation reserve balance and the capital adjustment account balance brought forward from the prior year.

Correcting for these misstatements would have resulted in the Council reporting a £101,000 higher surplus for the year. We considered that these misstatements did not have a material impact on our opinion on the financial statements.

Other matters we report on

Annual Governance Statement

We were satisfied that the Annual Governance Statement was not misleading or inconsistent with other information we were aware of from our audit.

Narrative reporting

Local authorities are required to include a Narrative Report in the Statement of Accounts to offer interested parties an effective guide to the most significant matters reported in the accounts. The Narrative Report should be fair, balanced and understandable for the users of the financial statements.

We were satisfied that the information given in the Narrative Report for the year ended 31 March 2017 was not inconsistent with the financial statements.

FINANCIAL STATEMENTS
Continued

Internal controls

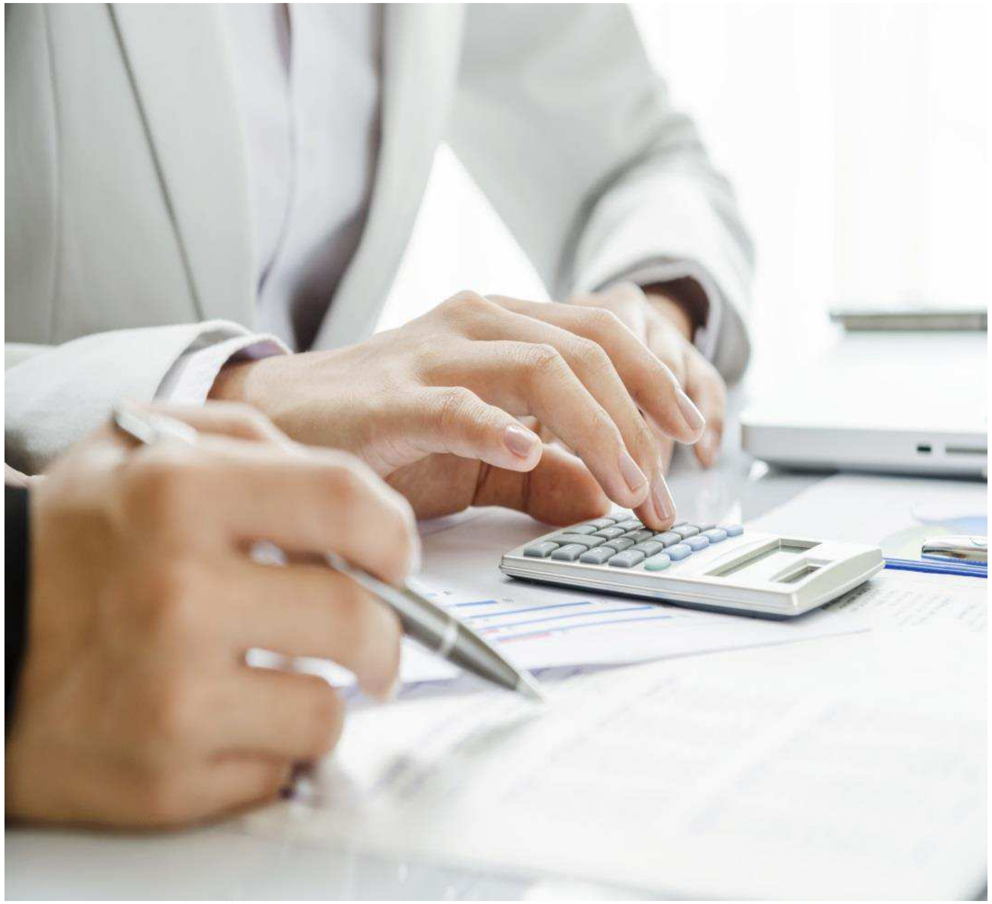
We did not find any significant deficiencies in internal controls during the course of our audit.

A few other areas for improvement were identified which we discussed with management. This included a recommendation for management to management to critically review the level of assets not revalued in the year on an ongoing basis.

Whole of Government Accounts

Auditors are required to review Whole of Government Account (WGA) information prepared by component bodies that are over the prescribed threshold of £350 million in any of: assets (excluding certain non current assets); liabilities (excluding pension liabilities); income or expenditure.

The Council falls below the threshold for review and there was no requirement for further work other than to submit the WGA Assurance Statement to the WGA audit team with the total values for assets, liabilities, income and expenditure. We submitted this on 29 September 2017, in advance of the national deadline.



USE OF RESOURCES

CONCLUSION	We issued an unmodified conclusion on the arrangements for securing economy, efficiency and effectiveness in its use of resources on 29 September 2017.

Scope of the audit of use of resources

We are required to be satisfied that proper arrangements have been made to secure economy, efficiency and effectiveness in the use of resources based on the following reporting criterion:

In all significant respects, the audited body had proper arrangements to ensure it took properly informed decisions and deployed resources to achieve planned and sustainable outcomes for taxpayers and local people.

As part of reaching our overall conclusion we considered the following sub criteria in our work: informed decision making, sustainable resource deployment, and working with partners and other third parties.

Our assessment of significant risks

Our audit was scoped by our knowledge brought forward from previous audits, relevant findings from work undertaken in support of the opinion on the financial statements, reports from the Council including internal audit, information disclosed or available to support the Annual Governance Statement and Narrative Report, information available from the risk registers and supporting arrangements, and other information brought to our attention during the course of the audit.

We set out below the risks that had the greatest effect on our audit strategy, the allocation of resources in the audit, and direction of the efforts of the audit team.

SUSTAINABLE FINANCES	RESPONSE	FINDINGS
The update to the Medium Term Financial Strategy (MTFS) to 2019/20 forecast further reductions in Government core grant funding, falling New Homes Bonus funding from 2017/18 and annual inflationary and pay award pressures. Budget gaps were identified in 2016/17 (£400,000), 2017/18 (£763,000), 2018/19 (£756,000) and 2019/20 (£617,000), resulting in an average level of required savings of £634,000 per annum over the four year period.	As a starting point for assessing the effectiveness of the Council's arrangements for ensuring sustainable finances, we reviewed current year outturn and the Council's reserves position.	The Council budgeted to spend £11.817 million on General Fund services in 2016/17 (incorporating a savings target of £685,000) and to make a net transfer to earmarked reserves of £780,000. The actual cost of services (before technical accounting adjustments) in 2016/17 was £11.646 million, an underspend of £171,000. The actual net transfer to reserves was £400,000 more than budgeted. With increased financing from business rates and Government grant, overall the general fund balance remained consistent with the prior year, at £2.06 million. The closing General Fund balance remains above the minimum level of £1 million recommended by the Section 151 Officer. The total Earmarked General Fund reserves balance fell by £623,000 to £10.096 million at 31 March 2017. The Council achieved efficiency savings and reduced expenditure of £677,000.

USE OF RESOURCES
Continued

SUSTAINABLE FINANCES	RESPONSE	FINDINGS
The Council currently has a number of major development / transformation programmes in place to either help facilitate these savings or create additional revenue streams in the medium term, to close the budget gaps. Our Audit Planning Report identified a risk that the MTFS may not adequately take account of the investment costs and savings associated with these projects, or that the Council may not have appropriate arrangements to monitor progress in delivering benefits from these projects against the MTFS.	We reviewed the assumptions used in the MTFS for investment costs and savings associated with major development/transformation programmes. We also reviewed the Council's arrangements for monitoring the progress of these programmes against the budgeted savings targets.	**Joint transformation programme with Eastbourne Borough Council** In November 2016, Cabinet approved a three phase delivery of the JTP, with phase one lasting from September 2016 to March 2017 for management and corporate activity to deliver £1.05 million of savings across the two councils. Phase two is taking place in 2017/18, covering frontline services and delivery of a further £1 million of savings, and phase three is expected to be in 2018/19 with an ongoing review of support services delivering £0.8 million of savings. Although the exact savings figure for Phase one will not be established until the final vacant roles are recruited, management expects to slightly exceed the savings target. Good progress has also been made on key technology projects to align the two councils. **North Street Quarter Development** Management expects this major capital project to bring over 400 new homes to the town, 40% of which will be affordable. This is a long term project which is still in the development phase. **Newhaven Enterprise Zone** This is a collaboration between Coast to Capital and the Council. The project aims to facilitate the economic regeneration of Newhaven. The zone officially commenced on 1 April 2017 and includes the creation of new commercial floor space and over 2,000 jobs. Although no financial gains have been realised from the scheme so far, this is a long term project which is expected to increase revenue to the Council through business rates and other ancillary services. **Housing investment and commercial development** In March 2017, Cabinet approved the establishment of a solely owned Lewes Housing Investment Company (LHIC) and a Joint Housing Investment Partnership, jointly owned with Eastbourne Borough Council. LHIC and Aspiration Homes LLP were incorporated on 4 July 2017 and 30 June 2017 respectively. The Council plans to carry out more commercial development through this structure, with the LLP acting as the asset holding vehicle for affordable housing developed through the commercial development programmes. Although there was no benefit realisation in 2016/17, it is expected to assist with the savings gap going forward. **Conclusion** We are satisfied that the MTFS takes accounts of the investment costs associated with the Council's major transformational projects, and once these scheme are further established, management should be in a better place to forecast all of the associated savings going forward.

USE OF RESOURCES
Continued

INFORMED DECISION MAKING	RESPONSE	FINDINGS
As part of the 2015/16 audit of use of resources, we reviewed the governance and arrangements relating to the “New Homes” project and identified scope for improvement in arrangements underpinning the project. We agreed an action plan with officers for lessons learnt to be applied to future projects of this size and nature including: • Earlier disclosure of potential development sites • Public consultation in preliminary stages • Updating the Property Strategy and Asset Management Plan • More structured approach to carrying out due diligence checks. The Council has a number of ongoing major capital projects. Our Audit Planning Report identified a risk that the Council may not have applied the lessons learnt from the New Homes project in planning for, and informing, its decision making on other significant capital projects.	We followed up on the progress made in addressing the action plan agreed as part of the 2015/16 use of resources audit in respect of significant capital projects.	Management has made considerable progress against the action plan from 2016/17, including the launch of the project management toolkit and corresponding training in July 2017, and adoption of a new asset management plan by Cabinet in June 2017. From discussion with the Head of Regeneration, we have assessed whether management has applied the lessons learnt from the New Homes project to the North Street Quarter project, which is currently in progress. The North Street Quarter is a project that has been going on for a number of years, and first initially went to Cabinet in 2013. Although the initial consultations were before the recommendations made in our prior year Audit Completion Report, some lessons learnt have still been applied to this project. The Council held considerable detailed public consultations prior to the planning application going in, in 2015. To ensure that the public engagement has continued, the Council has continued that process through a formal Sounding Board, as well as an Engagement Board on specific areas (design and landscape and play). The Council has set up a Members Oversight Board, made up of the lead members of the two main political groups. This board meets on an ad hoc basis, when key decisions are being made or at key project stages, with the board being engaged in the run up to any decisions. They also receive feedback on progress and updates on key project streams. These meetings are attended by the Corporate Management Team. There is clear evidence that our recommendations have been applied to the North Street Quarter, although this project was already in progress before the recommendations were agreed.

EXERCISE OF STATUTORY POWERS

Use of statutory powers

We have not exercised our statutory powers and have no matters to report.

REPORT BY EXCEPTION	We have no matters to report by exception.

Audit certificate

We issued the audit certificate to close the audit for the year ended 31 March 2017 on 29 September 2017.

GRANT CLAIMS AND CERTIFICATION

CERTIFICATION WORK	Our review of grant claims and returns for 2016/17 is in progress and the results will be reported upon completion of this work.

Housing benefit subsidy claim

Public Sector Audit Appointments Ltd has a statutory duty to make arrangements for certification by the appointed auditor of the annual housing benefit subsidy claim.

Our audit of the 2015/16 housing benefits subsidy claim identified a particularly high level of error within the cases tested, across all claim types. Our work was completed and the claim was certified on 5 July 2017 and details of the identified errors were reported to the Audit and Standards Committee on 25 September 2017. Our audit certification was qualified and we quantified the effect of the errors identified on the Council's entitlement to subsidy in a letter to the Department for Work and Pensions (DWP). DWP communicated the outcome to the Council on 31 July 2017, reducing the final subsidy amount by a net total of £4,609.

Our work on the 2016/17 housing benefits subsidy claim is currently in progress. The deadline for the completion of this work is 30 November 2017 however discussions with officers have indicated that this work is likely to be delayed again due to the level of errors encountered in previous years, and the additional work required to address this. We remain in dialogue with the Council with the aim of completing this work as early as practically possible.

Pooling of housing capital receipts return

The Council has requested that we undertake a 'reasonable assurance' review, based on the instructions and guidance provided by the Department of Communities and Local Government (DCLG), for its pooling of housing capital receipts return for 2016/17. The deadline for completion of this work is 31 October 2017.

This assurance review is undertaken outside of our appointment by Public Sector Audit Appointments Ltd, and is instead covered by a tripartite agreement between the Council, DCLG and the auditor.

Our review of the 2016/17 return was completed before the deadline and identified no significant issues.

APPENDIX

Reports issued

We have issued the following reports since our previous Annual Audit Letter.

Reports issued

We have issued the following reports since our previous Annual Audit Letter.

Fees

We reported our original fee proposals in our Audit Planning Report.

REPORT	DATE
Audit Planning Report 2016/17	27 February 2017
Planning Letter 2017/18	18 April 2017
Grant Claims and Returns Certification 2015/16	13 September 2017
Audit Completion Report 2016/17	13 September 2017
Audit Completion Report 2016/17 (Updated)	28 September 2017
Annual Audit Letter 2016/17	30 October 2017

AUDIT AREA	PLANNED FEES	FINAL FEES
Code audit	46,418	46,418
Additional audit fee	1,000	500(1)
Certification of housing benefits subsidy	15,598	14,960(2)
Fee for audit services	63,016	61,878
Audit related services:		
- Pooling of housing capital receipts	1,500	1,500(2)
Fee for audit related services	1,500	1,500
Other non audit related services:		
- None	-	-
Total fees	64,516	63, 378

(1) Additional fee for follow up of the Council's progress in addressing recommendations following our review of the New Homes project in 2015/16. Due to assistance of internal audit in completing this work, we reduced this fee down to £500. This additional fee is still subject to approval by PSAA.

(2) This fee is based on the 2015/16 fee. Fees for our grant certification work will be finalised following completion of the work.

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