GOVERNANCE COMMITTEE

Meeting of the GOVERNANCE COMMITTEE to be held in the Fire Authority Rooms at the Fire and Rescue Service Headquarters, Nissan Way, Barmston Mere, Sunderland on MONDAY, 21st MARCH, 2011 at 10.30 a.m.

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DAVE SMITH,
Clerk to the Authority.

11th March, 2011.

Item 3

Minutes of the meeting of the GOVERNANCE COMMITTEE held in the Fire and Rescue Service Headquarters, Barmston Mere on MONDAY 27 SEPTEMBER 2010 at 10.30 am

Present:

Mr. J.P. Paterson in the Chair

Councillors Charlton, Clark, M. Forbes, Haley and Woodwark.

In Attendance:-

Steve Nicklin	-	District Auditor
Lynn Hunt	-	Audit Commission

Apologies for Absence

Apologies for absence were submitted to the meeting on behalf of Mr. Cook and Miss Goodwill.

Declarations of Interest

There were no declarations of interest.

Minutes

7. RESOLVED that the minutes of the last meeting held on 28 June 2010 be confirmed and signed as a correct record.

In response to a question Councillor M. Forbes asked at the last meeting relating to how many ethnic minority staff were employed, the Chief Fire Officer advised that there were currently 32 out of 1200 with an additional two currently attending the training course.

Abolition of Standards for England

The Deputy Clerk submitted a report informing Members that the Government's "Programme of Government" of 20 May 2010 contained a commitment to "abolish the Standards Board Regime".

Members of the Committee were advised that Royal Assent was expected between July and October 2011. This being likely to result in the closure of the organisation between January and March 2012. In the meantime, the local standards framework still existed. Standards for England planned to continue to fulfil its statutory duties and Standards Committees and Monitoring Officers had an obligation to keep the system operating.

It was:-

8. RESOLVED that the contents of the report be noted.

Audited Statement of Accounts 2009-10

The Finance Officer submitted a report which included the Letter of Representation, the Audit Commission's Annual Governance Report relating to the Financial Statements and the Audited Statement of Accounts for the financial year ended 31 March.

Referring firstly to the Letter of Representation (attached at Appendix A), Members were provided with assurances from both the Authority and Sunderland City Council that the financial statements submitted gave a true and fair view of the financial position of the Authority as at 31 March 2010 and its income and expenditure for the year then ended. This document was signed by the Finance Officer.

Lynn Hunt and Steve Nicklin then took Members of the Committee through their Annual Governance Report (Appendix B) and advised of their intention to issue an audit report including an unqualified opinion on both the financial statements and value for money.

Although the Authority had been faced with complex changes to Local Government accounting requirements, the financial statements had been prepared to a high standard. Officers had made some amendments as a result of the Auditor's work, but none of these impacted upon the Authority's financial performance for the year, or the levels of reserves and balances.

In relation to value for money, all of the relevant criteria had been met and the Authority continued to manage its finances effectively, whilst at the same time delivering efficiencies and improved outcomes in key areas of activity.

Turning then to the Statement of Accounts 2009/10 (Appendix C), Members were advised that following the audit, the accounts had been amended, for a number of presentational issues, which were set out at Appendix 1, for information.

Councillor Haley referred to the pension interest cost within the Accounts and queried the underspend. The Finance Officer responded by explaining the way in which estimates were drawn up and how changes in valuations affect the Pension Fund. As factors influencing this included, for example, membership and longevity, estimates were only ever of a snapshot in time.

Members of the Committee then commented that they were pleased with the report, and congratulated Officers on the findings.

It was:-

9. RESOLVED that:-

(i) the Letter of Representation be noted;

(ii) the contents of the Audit Commissioner's Annual Governance report relating to financial statements be noted; and

(iii) the amended Audited Statement of Accounts for the financial year ended 31 March 2010 be approved.

Treasury Management – Half Yearly Review of Performance 2010/2011

The Finance Officer submitted a report on the borrowing and Investment Strategy and Performance for 2010/2011 to date, which incorporated the first and second quarterly Treasury Management Reviews.

Members were advised that the Authority was operating within its Authorised Borrowing limit and that there were no areas of concern.

Interest rate forecasts were expected to increase over the next three financial years from its current level of 0.50% to 1.5% by March 2011 and 4.50% by March 2013. As a result, a benchmark financing rate of 4.50% for long-term borrowing was set for 2010/2011.

The Finance Officer advised that with regards to investment, a rate of return of 1.43% had been achieved compared with the benchmark rate of 0.40%. The Investment Policy was currently being monitored to ensure it had flexibility to take full advantage of changes in market conditions.

In view of the current economic climate, the Finance Officer had been given delegated authority to vary the Lending List Criteria and the Lending List itself, should circumstances dictate. These were set out at Appendix A and B of the report and included any changes.

The borrowing strategy for 2010/2011 made provision for debt rescheduling but it would be difficult to refinance long term loans at interest rates lower than those already in place. As a result, no debt rescheduling had been undertaken during 2010/11 as rates had not been considered sufficiently favourable.

Loans totalling 30.5 million had been taken out within the current financial year at favourable rates across a range of periods and within the Authority's target rate of 4.50%.

It was:-

10. RESOLVED that the Treasury Management Performance for 2010/2011, to date, be noted.

Internal Audit Services – 2010/2011 Audit Plan Progress Report

The Head of Internal Audit submitted a report to consider the performance of Internal Audit up to 13 August 2010, the areas of work undertaken, and the Internal Audit opinion regarding the adequacy of the overall system of Internal Control within the Authority.

The work planned for the year included five audits. Two were now complete (Stores and Information Governance at the Emergency Planning Unit), one was ongoing and should be completed by September (Procurement) and the timing of the final two audits had been agreed and would be scheduled in consultation with the relevant managers.

Summarising the Internal Audit work, 20 medium risks were identified and 2 low. Of the 20 medium risks, 14 related to the Information Governance arrangements within the Emergency Planning Unit, where overall arrangements were considered to be unsatisfactory. Recommendations had now been agreed and a follow up audit planned for later in the year to review progress.

The Deputy Chief Emergency Planning Officer assured Members of the Committee that issues were being addressed and policies put in place.

It was:-

11. RESOLVED that the Internal Audit's performance be noted together with the overall opinion throughout the Authority that there continued to be a sound internal control environment.

International Financial Reporting Standards – Progress Report

The Finance Officer submitted a report providing Members of the Committee with an update on the Authority's progress made towards compliance with International Financial Reporting Standards (IFRS) since the initial report made to Committee on 22 March 2010.

Phase 1 was completed by 31 July. A detailed timetable for Phase 2 was about to be finalised, with Phase 3 being managed through the final accounts closure timetable for 2010/2011.

Members were referred to Appendix 1 of the report which outlined the timescale for restating the 2009/10 Statement of Accounts (Phase 2). The main area of concern being that the final guidance on the format of the 2009/2010 IFRS accounts was yet to be released by CIPFA.

A timetable for Phase 3 – production of IFRS complaint accounts for 2010/2011 would be prepared in December. During this phase, relevant Members and Officers would be trained on the specific requirements of IFRS to enable appropriate scrutiny of the revised Statement of Accounts for 2010/2011, to be presented to the Committee in June 2011.

Members were assured that progress to date had been good, with no deviations expected from the timetable at this time. Regular progress reports would continue to be submitted to the Committee.

It was:-

12. RESOLVED that the report and project outline set out at Appendix 1 of the report, be noted.

TYNE & WEAR FIRE AND RESCUE AUTHORITY **Item 4**

MEETING: 21 MARCH 2011

ANNUAL REPORT ON THE WORK OF THE COMMITTEE ON STANDARDS ISSUES

REPORT OF THE DEPUTY CLERK

1. Introduction

This is the third annual report to have been prepared on the work of the Committee, on standards matters.

In previous years, the report has been used to complete the annual return questionnaire issued by Standards for England. Whilst there is no longer a requirement to submit a return, the report has been prepared for Members' information.

2. Membership

The Committee is comprised as follows:-

6 Members (Councillors Bell, Clark, Haley, M. Forbes, Charlton and Woodwark).

3 Independent Members (Mr. G.N. Cook – Chairman,
Mr. J.P. Paterson – Vice Chairman and Miss G. Goodwill).

3. The role of the Standards Committee

The main purpose of the Committee is to promote and maintain high standards of conduct by Members, including Co-optees. The detailed terms of reference are set out in the Authority's Constitution.

4. Meetings

The full Committee will have held 3 meetings during the course of the year.

5. Matters Considered

Like other Fire and Rescue Authorities with relatively small membership, there have been no matters of concern raised or hearings held in the last year.

The Committee has considered a report on the Government's proposal to overhaul the Standards regime and a further update is included on this agenda. Elsewhere on this agenda there is also a report regarding the endorsement of a Partnership Behaviour Protocol.

6. Local Assessments

There have been no local assessments. However, four Members of the Committee have general experience of these through their role on Sunderland City Council's Standards Committee.

7. Register of Interests

In the interests of transparency, the register of interests continues to be available to be accessed electronically on the Authority's website.

Members are sent a copy of their interests during the course of the year to check that their entries are up to date.

8. Conclusion

The Committee is requested to note the report.

PREVENTING PROTECTING RESPONDING

TYNE AND WEAR FIRE AND RESCUE AUTHORITY

MEETING: 21 MARCH 2011

SUBJECT: REVIEW OF THE STANDARDS REGIME

REPORT OF THE CLERK TO THE AUTHORITY

1. Members will recall receiving a report at the meeting of the committee held on the 27th September 2010 regarding the Government's proposal to abolish the Standards Board regime. The purpose of this report is to provide a brief update to the Committee with regard to the proposals.

2. Provision is included in the Localism Bill to abolish Standards for England, the requirement for authorities to have Standards Committees and the National Code of Conduct.

   As currently drafted, in place of the Standards Board regime, the Bill provides that authorities will have a duty to promote and maintain high standards of conduct by Members and will be able to establish their own voluntary codes of conduct. Where an authority adopts a Code of Conduct, it may investigate any complaint that it has been breached, however, at present, there are no protocols or guidance on how to go about this. If an authority does not adopt a code of conduct, there is no provision in the Bill for allowing an investigation of complaints about Member conduct which would suggest that in the absence of a Code, the only way of sanctioning poor behaviour would be through the criminal law, where possible, or appeals to the Ombudsman.

3. There is also provision to the effect that regulations may require monitoring officers to establish and maintain a register of interests, specify those interests which must be registered and disclosed by members, prevent or restrict members' participation in business if they have an interest, allow for authorities to provide for dispensations and provide for sanctions. The Bill proposes a new offence of non-compliance with the registration regulations, which could result in a fine or disqualification. Prosecutions must be brought by or on behalf of the Director of Public Prosecutions.

4. Members will be advised of further developments as the Bill progresses through Parliament and any further detail becomes available as to any proposed regulations and guidance.

Recommendation

That the Committee notes this report.

Background Paper
Localism Bill

Creating the Safest Community

PREVENTING PROTECTING RESPONDING

TYNE AND WEAR FIRE AND RESCUE AUTHORITY

MEETING: 21 MARCH 2011

SUBJECT: PARTNERSHIP BEHAVIOUR PROTOCOL

REPORT OF THE CLERK TO THE AUTHORITY

1. Introduction

The purpose of this report is to inform the Committee of a Partnership Behaviour Protocol which has been developed by Standards for England.

2. Partnership Working

Partnership working between public authorities and other agencies is now integral to the future of policy development and service delivery for the public sector. At a national level the Government is increasingly promoting joint working/shared services. Standards for England has recognised the increasingly important aspect of partnerships to public service delivery and the importance of good governance of partnership arrangements to enable an authority to operate more effectively and to manage risk.

Partners who are not members of an authority are not subject to the same rules governing their behaviour as elected or co-opted Members of an authority and therefore to help address this, Standards for England has developed a Partnership Behaviour Protocol, which is set out in the Appendix to this report.

3. Partnership Behaviour Protocol

The protocol is consistent with the CIPFA Solace (Chartered Institute of Public Finance and Accountancy / Society of Local Authority Chief Executives) Good Governance Framework and the general principles for the conduct of people in public life which are set out in the Relevant Authorities (General Principles) Order 2001 and reflected in the preamble to the Authority's Code of Conduct.

Standards for England states that the protocol aims to:

- embed high ethical standards and partnership working
- address the disparity of rules and scrutiny governing those involved in local decision making
- enable partners to agree what behaviour they can expect from each other
- help partners hold each other to account and encourage constructive challenge between partners

- help partners to exercise leadership by demonstrating their own high standards of behaviour to other partners and to the public
- promote trust amongst the general public, demonstrating the partners' commitment to behaviour of a certain standard
- improve performance management

It is suggested that the Protocol could be used to assess the compatibility of partners by asking them to sign up to some common values and behaviours and could also be used as part of a tendering process, under which potential partners could be asked if they would be willing to sign up to and provide evidence of the values specified. The Protocol can be adapted, as appropriate, to fit local circumstances.

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4. Recommendation

It is recommended that the Partnership Behaviour Protocol be commended to the Authority and that as part of the process of inviting tenders and/or developing future partnership arrangements, in each case consideration is given to the option of incorporation of the protocol, adapted as appropriate, to fit the circumstances.

Background Paper

Protocol on Local Authority Partnership Working published by Standards for England

Partnership behaviour protocol

Achieve intended outcomes

Our priorities are evidence based and our decision making is transparent.

We will:

- Share resources to achieve joint outcomes
- Monitor how well we have used our resources
- Actively encourage ideas and innovation
- Ensure that decision making is transparent
- Be committed to continuous improvement
- Ensure that claims of improved performance are based on clear evidence
- Establish accountability both across the partnership (horizontally) and within each organisation (vertically)

Public interest

We act in the interest of the public and demonstrate value.

We will:

- Focus on long term as well as short term issues
- Act in the interests of the public good over individual interests
- Demonstrate to the community how we are achieving publicly valued outcomes
- Agree a protocol for the handling of complaints that relates to our joint work

Building partners' capacity

We build capacity in our partnership.

We will:

- Be committed to developing individual partners' skills to achieve our aims
- Encourage partners to be confident working outside of their organisational culture
- Be open to partners' suggestions and help

Value and respect each other

We respect and value everyone's contribution.

We will:

- Ensure that all partners contribute appropriately and openly
- Acknowledge the capabilities of all members
- Recognise and embrace the role of voluntary and community sector partners
- Avoid dominance by one or two individuals
- Respect each other's roles and needs
- Actively encourage the participation of all partnership members
- Build effective working relationships with each other
- Recognise the value of all partners' contributions

Act ethically

We act ethically. We are open and objective and encourage constructive challenge.

We will:

- Agree a mechanism for whistleblowing and dealing with complaints
- Ensure whistleblowers are supported
- Actively promote a 'no-blame' culture
- Support partners to both understand and constructively challenge any poor behaviour
- Use appropriate, unambiguous and simple language
- Agree how we will achieve democratic accountability
- Ensure that our dialogue is open and transparent
- Declare conflicts of interest and address them
- Make sure that the purpose of all meetings is made clear
- Be honest and objective

Aligning strategies and networks

We harness our collective efforts through joint planning, delivery and governance arrangements.

We will:

- Ensure that partners can influence the decision making of member organisations
- Allow sufficient time and capacity to be given to understand an issue and to reflect on its impact
- Make sure that actions taken by the partnership are clear, time-limited and task-orientated
- Encourage all partners to actively shape the strategy
- Ensure that agreed actions are carried out

PREVENTING PROTECTING RESPONDING

TYNE AND WEAR FIRE AND RESCUE AUTHORITY **Item 7**

MEETING: 21 MARCH 2011

SUBJECT: ANNUAL AUDIT LETTER, 2009/2010

JOINT REPORT OF THE CHIEF FIRE OFFICER, CLERK TO THE AUTHORITY AND FINANCE OFFICER

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1. INTRODUCTION

1.1 This report provides the Committee with an outline of the content of the Audit Commission's Annual Audit and Inspection Letter for 2009/2010 in respect of Tyne and Wear Fire and Rescue Authority (a copy of the main body of the Audit and Inspection Letter is attached as Appendix A for information).

1.2 Officers of the Audit Commission will be attending the meeting to present the key findings of the report and to answer any questions that may arise.

2. BACKGROUND

2.1 As Committee members will be aware, each year the Authority receives an Annual Audit Letter from its external auditors setting out how effectively the Authority has performed over the year and succeeded in achieving value for money. To this end, the Annual Audit Letter for the 2009/2010 year has been received by the Chief Fire Officer who has provided a brief outline of the content of the report.

2.2 The main body of the Annual Audit Letter has been structured into five sections, together with two appendices. The five sections in the main body of the Audit Letter are as follows;

- Key messages
- Financial statements and annual governance statement
- Value for money
- Current and future challenges
- Closing remarks

3. KEY MESSAGES

3.1 The Key Messages section provides a précis of the content of the report and the Chief Fire Officer is of the opinion that the following items are particularly worthy of note.

Creating the Safest Community

3.2 An unqualified audit opinion on the Authority's 2009/2010 financial statements has been issued by the auditors together with an unqualified Value for Money conclusion.

3.3 The Letter also states that the Authority's financial statements and supporting working papers were prepared to a good standard despite the introduction of complex changes to the accountancy arrangements which officers of the Authority had address.

3.4 The Letter also highlights the fact that the Authority continues to manage its finances in an effective manner and that both costs and performance have generally improved when compared to the other metropolitan fire and rescue authorities. In particular there have been continued reductions in accidental and deliberate primary fires as well as high levels of public satisfaction with the service being recorded.

4. CURRENT AND FUTURE CHALLENGES

4.1 Not surprisingly the Audit Letter highlights the fact that the Authority is facing a 25% reduction in formula grant funding over the four year period covering 2011/2015 and acknowledges that this will present challenges to all concerned.

4.2 Additionally, the Letter also highlights the importance of maintaining the Authority's existing performance management arrangements in order to ensure that the services that are currently available continue to be provided effectively and that any new initiatives can been properly monitored for their impact.

4.3 Taking into account these challenges, the Audit Letter highlights the ongoing need for strong and focused leadership as the service starts to address the unprecedented financial pressures that are rapidly approaching.

5 RECOMMENDATIONS

5.1 The Committee is requested to:-

a) consider the content of the Annual Audit and Inspection Letter for 2009/2010 and;

b) receive further reports as appropriate.

BACKGROUND PAPERS

The undermentioned Background Papers refer to the subject matter of the above report:

- Annual Audit Letter 2009/2010.

Annual Audit Letter

Tyne and Wear Fire and Rescue Authority

Audit 2009/10

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

Contents

Key messages

This report summarises my findings from the 2009/10 audit. My audit comprises two elements:

- **the audit of your financial statements (pages 5 to 6); and**
- **my assessment of your arrangements to achieve value for money in your use of resources (pages 7 to 9).**

Financial statements

1 The Authority has been faced with complex changes to its accounting requirements in 2009/10, in spite of this the standard of financial statements and supporting working papers were good. Although there were a number of amendments as a result of our audit work, none of these had any impact on the Authority's reported financial performance for the year, or the levels of reserves and balances previously notified to Members.

2 I issued an unqualified opinion on the financial statements on 30 September 2010, in line with statutory requirements.

Value for money

3 All of the relevant value for money criteria specified by the Audit Commission for fire and rescue authorities have been met. I issued an unqualified value for money conclusion as part of my audit opinion and certificate on 30 September 2010.

4 The Authority continues to manage its finances effectively, and has maintained the strengths we identified last year in relation to financial planning and reporting, internal control, governance and partnership working. We also noted a number of improvements. Performance monitoring and management has improved through better use of incident reporting information and an increased willingness to challenge established ways of doing things.

5 Costs and performance have generally improved relative to other metropolitan fire services, with continued reductions in the numbers of deliberate and accidental primary fires, and high levels of public satisfaction with the service.

6 Inevitably there remains some scope for improvement. Deliberate secondary fires remain high compared with other metropolitan fire authorities, as do automatic fire alarm call-outs. The Authority has put arrangements in place to analyse in detail the intelligence linked to such incidents, and has introduced practical initiatives to reduce them, working in partnership with others.

Audit fees

7 An analysis of our audit fees for 2009-10 is set out in Appendix 1. There have been no changes to fee levels previously agreed with you.

Current and future challenges

8 The scale of financial pressures facing public bodies in the current economic climate is unprecedented in recent years. The Authority is currently reformulating its plans and priorities in the light of recent Government announcements that there will be a 25 per cent reduction in formula grant funding for fire and rescue authorities over the period to 2014/15.

9 At the same time, the absence of a nationally determined framework for comparative information and assessment will put the onus on the Authority's own performance management processes to:

- identify and implement improvements; and
- ensure that agreed service standards are maintained.

10 This has been recognised and is to be addressed through participation in the Local Government Group, regional and national fire networks. There will also be a number of operational challenges to deal with, and much still remains to be done, both at a national and local level, to progress the regional control centre project.

11 Against this background, demands placed on management will be significant and capacity inevitably stretched. Members will need to:

- provide strong and focussed leadership;
- make difficult decisions when necessary;
- ensure that deliverable forward plans are in place; and
- develop robust monitoring procedures to ensure that these are delivered.

Financial statements and annual governance statement

The Authority's financial statements and annual governance statement are an important means by which the Authority accounts for its stewardship of public funds.
I gave an unqualified opinion on the Authority's 2009/10 financial statements on 30 September 2010, in line with statutory target dates.

Overall conclusion from the audit

12 The Authority has been faced with complex changes to its financial reporting requirements in 2009/10. Areas most affected were fixed asset and agency accounting, and new disclosures for senior officer remuneration. Overall the Authority coped well with these new requirements. Financial statements and working papers were prepared to a good standard and officers responded promptly to our queries and requests for further information.

13 Officers did agree to make the following adjustments as a result of our audit work :

- amendments to the Cash Flow Statement and comparative information in respect of agency accounting;
- additional disclosures in respect of recent pension changes, retained firefighter back pay awards and the future financial obligations in respect of PFI Phase 2 (Tynemouth Fire Station);
- additional information and explanations in respect of officers' emoluments disclosures; and
- various other presentational adjustments to the Balance Sheet, Firefighters' Pension Fund Account and disclosure notes.

14 None of these amendments had any impact on the Authority's financial performance for the year, or the levels of reserves and balances previously reported to Members.

Significant weaknesses in internal control

15 I did not identify any significant weaknesses in the Authority's internal control arrangements.

Preparations for IFRS

16 A major challenge for all local authorities is the move to International Financial Reporting Standards (IFRS). Changes to the accounting treatment for PFI schemes and agency arrangements have already been implemented. Issues to be addressed in 2010/11 relate to:

- leasing;
- employee benefits; and
- valuations and disclosures in respect of property, plant and equipment.

17 Work in respect of all of these areas is well in hand and Members have received regular progress reports. The next key stage for officers is to restate the 2009/10 opening balance sheet position and devise a skeleton set of 2010/11 accounts. We intend to review these early in 2011.

Value for money

I considered whether the Authority is managing and using its money, time and people to deliver value for money.
I assessed your performance against the criteria specified by the Audit Commission and have reported the outcome as the value for money (VFM) conclusion.

2009/10 use of resources assessments

18 At the end of May 2010, the Audit Commission wrote to all chief fire officers to inform them that following the Government's announcement, work on CAA would cease with immediate effect and the Commission would no longer issue scores for its use of resources assessments.

19 However, I am still required by the Code of Audit Practice to issue a value for money conclusion. I have therefore used the results of the work completed on the use of resources assessment up to the end of May to inform my 2009/10 conclusion.

20 I report the significant findings from the work I have carried out to support the vfm conclusion.

VFM conclusion

21 I assessed the Authority's arrangements to achieve economy, efficiency and effectiveness in its use of money, time and people against criteria specified by the Audit Commission. The Audit Commission specifies each year, which Key Lines of Enquiry (KLOE) are the relevant criteria for the VFM conclusion at each type of audited body.

22 A summary of my findings is set out below.

Criteria	Adequate arrangements?
Managing finances	
Planning for financial health	Yes
Understanding costs and achieving efficiencies	Yes
Financial Reporting	Yes
Governing the business	
Commissioning and procurement	Yes
Use of information	Yes
Good governance	Yes
Risk management and internal control	Yes
Managing resources	
Natural Resources	Yes

23 The Authority has maintained the strengths we identified last year in relation to financial planning and reporting, internal control, governance and partnership arrangements. We also noted a number of improvements, as follows:

- Performance monitoring and management has developed significantly, with a performance action group established to improve accountability and share best practice. Detailed incident reports at district and station level have enabled more focussed preventative activity. As a result, kitchen fires have reduced by 11 per cent and antisocial behaviour fires by 57 per cent.
- Costs and performance have generally improved relative to other metropolitan fire services, with continued reductions in the numbers of deliberate and accidental primary fires, high levels of public satisfaction with the service, better targeting of preventative and community safety work and generally good outcomes from partnership initiatives. All key activity objectives have been met.
- There is increasing willingness to challenge established ways of doing things, with rigorous cost/benefit analysis and an expectation that all staff will identify and deliver efficiencies within their own service areas. Back office functions have also been reviewed using 'lean thinking' techniques.

24 Management of natural resources was assessed as a value for money criteria for the first time in 2009/10. The Authority displays a clear commitment to managing its impact on the environment, and has delivered a number of successful outcomes in this area.

25 Inevitably there remains some scope for improvement. Deliberate secondary fires remain high compared to other metropolitan fire authorities, as do automatic fire alarm call-outs, and the Authority has plans in place to tackle these areas in the coming the year.

Local risk-based work

26 To support my review of the criteria set out above I have continued to track progress on the regional control centre. The North-east project is one of a number of pilot projects nationally, aiming to replace individual fire service control centres with up to date regional facilities. But the projects, which are 100 per cent government funded, have experienced considerable difficulties and delays.

27 Independent reviews by both the Parliamentary Accounts Committee and the National Audit Office this year were highly critical but concluded that better value for money would be achieved by completing the projects than by curtailing them. New contractors have been appointed with clearer deadlines, key milestones and more onerous contract penalties established.

28 At a local level the four north east fire authorities have worked together to progress the project as well as could be expected. In the absence of any national guidance they have managed to:

- develop a common set of locally agreed service standards and response procedures;
- assess staffing needs, TUPE implications and redeployment opportunities; and
- agree on the joint venture accounting treatment.

29 Tyne and Wear Fire and Rescue Authority has also set aside some additional financial resource to cover any future shortfalls in Government funding. But clearly many uncertainties remain, and much is still left to do at both national and local levels.

Approach to local value for money work from 2010/11

30 Given the scale of pressures facing public bodies in the current economic climate, the Audit Commission has been reviewing its work programme for 2010/11 onwards. This review has included discussions with key stakeholders of possible options for a new approach to local value for money (VFM) audit work. The Commission aims to introduce a new, more targeted and better value approach to our local VFM audit work.

31 My work will be based on a reduced number of reporting criteria, specified by the Commission, concentrating on:

- securing financial resilience; and
- prioritising resources within tighter budgets.

32 I will determine a local programme of VFM audit work based on my audit risk assessment, informed by these criteria and my statutory responsibilities. I will no longer be required to provide an annual scored judgement relating to my local VFM audit work. Instead I will report the results of all my local VFM audit work and the key messages for the Authority in my annual report to those charged with governance and in my annual audit letter.

Current and future challenges

Financial pressures

33 Tyne and Wear Fire and Rescue Authority manages its finances well, and has developed a much clearer focus on value for money in recent years. In 2009/10 it completed a comprehensive review of back office services and reported efficiency savings well in excess of national targets. A culture has been successfully developed whereby all staff take responsibility for identifying and delivering efficiencies in their own service areas

34 But financial pressures are increasing at an unprecedented rate. The Government's recent spending review has indicated that there will be a 25 per cent reduction in formula grant funding for fire and rescue authorities over the period to 2014/15, equivalent to a 13 per cent reduction in 'real terms' resourcing. Interest income from investments has plummeted, at the same time interest rates on PWLB loan payments are expected to rise.

35 The Authority is reformulating its financial plans and priorities in the light of these proposals. An updated medium term financial plan and budget planning framework are due to be presented to members for approval in December 2010, and work is under way to produce a draft budget for 2011/12 early in the New Year.

36 The Authority recognises that the future may demand more difficult choices and changes to the established patterns of service provision. It may also wish to reconsider the future use of longstanding earmarked reserves and provisions in the light of changing circumstances.

Improving performance

37 The Government has recently announced the abolition of:

- CAA and Use of Resources;
- National indicators; and
- Local area agreements and stretch targets.

38 Many welcome this as an opportunity for public sector organisations to set their own agenda and focus on locally determined priorities and objectives. But the absence of a nationally determined framework for comparative information and assessment raises important questions for fire service managers about how the Authority will continue to identify and implement improvements in the future. It is also likely to have an impact on the role of:

- Members, especially those charged with governance and scrutiny roles; and
- Internal Audit, who may be able to provide additional assurance to management on governance, risk management and the quality of performance information.

39 This has been recognised and is to be addressed through participation in the Local Government Group, regional and national fire networks.

Future developments

40 The Authority is reasonably well placed financially, but recognises that the financial pressures it will face in the future may demand more difficult choices and changes to the established patterns of service provision. This is being reflected in the medium term financial plan. At the same time it will be facing a number of operational challenges, particularly in relation to the progress of the regional control centre.

41 Our future work will focus on financial resilience, delivery of identified efficiency savings, and improvements to value for money. We will also review the Authority's response to national publications such as the recent Audit Commission report on contingency arrangements.

Closing remarks

42 I have discussed and agreed this letter with the Chief Fire Officer and Chief Finance Officer and presented it to the Governance Committee. Copies have been made available for all Members.

43 Full details of the reports I have issued to the Authority during the year are set out below. Officers and Members have also received a number of verbal reports on emerging issues.

Report	Date issued
2009-10 Opinion Audit Plan	March 2010
2010/11 Audit plan	April 2010
■ Annual governance report ■ Auditor's report giving an opinion on the financial statements ■ External audit opinion on Whole of Government Accounts Return	September 2010

44 The Authority has taken a positive and helpful approach to our audit. I wish to thank staff for their support and cooperation during the audit.

Steve Nicklin
District Auditor

November 2010

Appendix 1 – Audit fees

	Actual	Proposed	Variance
Financial statements, annual governance statement and Whole of Government accounts return	£37,000	£37,000	0
Value for money	£37,200	£37,200	0
Total audit fees	£74,200	£74,200	0
Non-audit work	0	0	0
Total	£74,200	£74,200	0

Appendix 2 – Glossary

Annual governance statement

Governance is about how local government bodies ensure that they are doing the right things, in the right way, for the right people, in a timely, inclusive, open, honest and accountable manner.

It comprises the systems and processes, cultures and values, by which local government bodies are directed and controlled and through which they account to, engage with and where appropriate, lead their communities.

The annual governance statement is a public report by the Authority on the extent to which it complies with its own local governance code, including how it has monitored the effectiveness of its governance arrangements in the year, and on any planned changes in the coming period.

Audit opinion

On completion of the audit of the accounts, auditors must give their opinion on the financial statements, including:

- whether they give a true and fair view of the financial position of the audited body and its spending and income for the year in question; and
- whether they have been prepared properly, following the relevant accounting rules.

Financial statements

The annual accounts and accompanying notes.

Qualified

The auditor has some reservations or concerns.

Unqualified

The auditor does not have any reservations.

Value for money conclusion

The auditor’s conclusion on whether the audited body has put in place proper arrangements for securing economy, efficiency and effectiveness in its use of money, people and time.

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- any director/member or officer in their individual capacity; or
- any third party.

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November 2010

TYNE AND WEAR FIRE AND RESCUE AUTHORITY **Item 8**

MEETING: **GOVERNANCE COMMITTEE**

DATE: 21 MARCH 2011

SUBJECT: AUDIT COMMISSION – AUDIT OPINION PLAN 2010/2011

REPORT OF THE CHIEF FIRE OFFICER AND THE FINANCE OFFICER

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1. INTRODUCTION

1.1 The Audit Commission has notified the Authority of the work that it is proposing to undertake in respect of the audit of the financial statements, and the value for money conclusion, for 2010/2011.

2. BACKGROUND

2.1 The attached document advises on the nature of the work to be undertaken as part of the Audit Opinion Plan 2010/2011 together with the scale of the fee for the audit and the assumptions that inform this figure.

2.2 It also identifies the specific areas that will be covered by the planned audit work, based upon a risk assessment process. These areas of work are set out in the attached document.

2.3 An officer of the Audit Commission will be in attendance at the Governance Committee meeting in order to outline the content of the Plan and to answer any questions that may arise.

3. RECOMMENDATIONS

3.1 The Committee is requested to note the Audit Commission's Opinion Plan report in relation to the work to be undertaken in 2010/2011, based upon the Commission's risk-based approach to audit planning.

BACKGROUND PAPERS

Audit Commission; Audit Opinion Plan 2010/2011

Audit opinion plan

Tyne and Wear Fire and Rescue Authority

Audit 2010/11

The Audit Commission is an independent watchdog, driving economy, efficiency and effectiveness in local public services to deliver better outcomes for everyone.

Our work across local government, health, housing, community safety and fire and rescue services means that we have a unique perspective. We promote value for money for taxpayers, auditing the £200 billion spent by 11,000 local public bodies.

As a force for improvement, we work in partnership to assess local public services and make practical recommendations for promoting a better quality of life for local people.

Contents

Introduction

1 This plan sets out the audit work that we propose to undertake for the audit of financial statements 2010/11. The plan is based on the Audit Commission's risk-based approach to audit planning. It reflects:

- audit work specified by the Audit Commission – in 2010/11 this includes mandated work on the National Fraud Initiative; and
- current national risks relevant to your local circumstances; and specific local risks.

Responsibilities

2 The Audit Commission's Statement of Responsibilities of Auditors and of Audited Bodies sets out the respective responsibilities of the auditor and the audited body. The Audit Commission has issued a copy of the Statement to every audited body.

3 The Statement summarises where the different responsibilities of auditors and of the audited body begin and end, and our audit work is undertaken in the context of these responsibilities. A working arrangements protocol has been agreed with you and is in place which sets out in detail how we discharge our relative responsibilities at a local level.

4 We comply with the statutory requirements governing our audit work, in particular the Audit Commission Act 1998 and the Code of Audit Practice.

Fee for the audit of financial statements

5 The fee for the audit is £75,000 as indicated in my letter of 26 April 2010. At this stage I am satisfied that fee remains appropriate. Further information on the basis for the fee is set out in appendix 1.

6 In setting the fee, I have assumed that:

- the Authority will prepare financial statements which comply with relevant requirements of International Financial Reporting Standards (IFRS), and CIPFA's 'Statement of Recommended Practice' (SORP) and
- good quality working papers will be supplied to support the financial statements.

7 Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee. We will discuss this in the first instance with the Chief Finance Officer, and we will issue supplements to the plan to record any revisions to the risk and the impact on the fee.

8 The Audit Commission have recently announced rebates to all audited bodies as part of a three-year programme to deliver cost reductions of about £70 million nationally. Rebates are from the Audit Commission centrally and not a reduction to the audit fee, although the amount of the rebate is based on audit scale fees. For Tyne and Wear Fire and Rescue Authority the rebate will be in the region of £1,100.

Specific actions the Authority could take to reduce its audit fees

9 The Audit Commission requires its auditors to inform audited bodies of specific actions it could take to reduce its audit fees. As in previous years, we will work with staff to identify any specific actions that the Authority could take and to provide ongoing audit support.

10 We will provide officers with a schedule of our detailed working paper requirements in advance of the post-statements audit.

Auditors report on the financial statements

11 I am required to issue an audit report giving my opinion on whether the accounts give a true and fair view of the financial position of the Authority as at 31 March 2011. As part of this opinion I am also required to consider:

- whether financial disclosures included in the Authority's annual report are consistent with the audited financial statements;
- whether disclosures made in the Annual Governance Statement (which forms part of the accounts) meet SORP requirements and are consistent with my knowledge of the Authority; and
- whether proper arrangements have been made by the Authority for securing economy, efficiency and effectiveness in its use of resources ('the value for money conclusion').

Identifying opinion audit risks

12 As part of our audit risk identification process, we need to fully understand the audited body to identify any risk of material misstatement (whether due to fraud or error) in the financial statements. We do this by:

- identifying the business risks facing the Authority, this includes an assessment of your own risk management arrangements;
- considering recent financial performance, and future prospects;
- assessing internal control – this includes reviewing the control environment, the IT control environment and Internal Audit; and
- assessing the risk of material misstatement arising from the activities and controls within key information systems.

Identification of specific risks

13 We have considered the key risks relevant to the 2010/11 opinion audit and these are set out below.

Table 1: **Specific opinion risks identified**

Risk area	Audit response
The Authority is required to implement IFRS requirements in full for the first time in 2010/11. Key changes relate to: ■ presentation and disclosure; ■ PPE (fixed asset) valuation and accounting; ■ lease arrangements; and ■ leave and holiday pay accruals.	We have already had early discussions with Finance staff regarding PPE valuations and component accounting. We will review the Authority's template for its 2010/11 accounts and opening balance restatement early in 2011 and we will undertake sample testing on material assertions in the accounts.

Risk area	Audit response
The Authority is required to comply with IFRIC12 requirements, and include the assets and associated liabilities of PFI schemes in its financial statements. Phase 1 PFI was brought on balance sheet last year and Phase 2 (Tynemouth Fire Station) a joint PFI scheme, will be included in the accounts for the first time in 2010/11.	We will review the accounting treatment of PFI schemes in the light of IFRIC12 and other guidance, seeking support from AC technical staff if necessary. We will compare assertions in the accounts to operators' financial models and review the allocation of costs and grant income on joint PFI schemes.
The Authority has interests in a limited company (NEFCCL). This needs to be accounted for in accordance with IFRS and SORP requirements.	We will ensure that the Authority's interest in NEFCCL is fully disclosed and properly accounted for, and consider the application of ISA (UK&I) 600 (group accounting). We will seek support from AC technical staff if necessary
The most significant and complex assertions in the accounts relate to PPE (fixed assets) and pensions obligations.	We will undertake appropriate testing to confirm these assets have been correctly valued and accounted for.
Sunderland City Council (SCC) provides support services, and treasury management, to the Authority.	We will plan and carry out our audit work in order to meet ISA (UK&I) 402 requirements. As part of this work we will: ■ liaise with the SCC external audit team; ■ undertake appropriate testing on material balances and transactions in the accounts; and ■ seek representations from management if necessary to confirm that shared costs and balances have been correctly allocated.

Testing strategy

14 On the basis of risks identified above we will produce a testing strategy which will consist of testing key controls together with substantive tests of transaction streams and material account balances at year-end. This testing will be carried out both before and after the draft financial statements have been produced (pre- and post-statement testing). The timing of our work and proposed site visits will be discussed in advance with officers.

15 Wherever possible, we will seek to rely on the work of Internal Audit to help meet our responsibilities, and to avoid the risk of duplicating audit effort.

The Clarity Project

16 My audit of the financial statements is governed by International Standards on Auditing (ISAs). As with all guidance and frameworks, auditing standards are revised and updated, often in a piecemeal fashion. However, in 2009 the auditing profession completed a comprehensive project to improve the clarity of all the ISAs. This is known as the Clarity Project.

17 One of the main objectives of the Clarity Project was to promote greater consistency of application between auditors. This has been done by reducing the ambiguity within existing ISAs and improving their overall readability and understandability.

18 The new clarified framework will apply to my audit of your 2010/11 financial statements. Because of the new standards, you may see some changes in the way my audit team delivers your audit and the information they seek from you. In appendix 3 I have set out the main changes and how they may impact on you.

The Value for Money Conclusion

19 . From 2010/11 auditors will not be required to provide annual scored judgements relating to their local VFM audit work. We will give our statutory value for money conclusion based on only two reporting criteria specified by the Commission and set out below:

Table 2: **Value for Money reporting criteria**

Specified reporting criteria	What the auditor will consider
The organisation has proper arrangements in place for securing financial resilience.	The organisation has robust financial systems and processes to manage effectively financial risks and opportunities, and to secure a stable financial position that enables it to continue to operate for the foreseeable future. The auditor will focus on the organisation's arrangements relating to financial governance, strategic financial planning and financial control
The organisation has proper arrangements for challenging how it secures economy, efficiency and effectiveness.	The organisation is prioritising its resources within tighter budgets, for example by achieving cost reductions and improving efficiency and productivity.

20 These criteria are in line with the expectations of the recent comprehensive spending review and proposed funding reductions for fire and rescue services.

21 There will be no key lines of enquiry for the specified criteria, and auditors are expected to determine the scope of their local programme of VFM audit work on the basis of their assessment of risk. The key risks that we have identified at this stage, and our proposed audit work, are set out below.

Table 3: **VFMC risk areas**

Risk area	Audit response
A focus on short term management at the expense of longer term financial planning	We will review up to date strategic and medium term financial plans, and the quality of data underpinning these.
The Authority may not maintain adequate arrangements to monitor achievement of key outcome targets and the impact of efficiencies on service quality and provision.	We will review 2010/11 value for money profiles and year-end performance reports.
Inadequate action to identify and deliver the required level of financial savings	We will review the corporate strategies for identifying and delivering financial savings, and the success of these arrangements to date.
Reluctance to challenge established processes or to explore innovative and new ways of delivering activities.	We will review outcomes delivered through service reviews and other management processes to date.
Lack of leadership on prioritising resources, and lack of consultation with staff, stakeholders and the public.	Minute reviews and discussions with key staff and elected members.

The audit team

22 The key members of the 2010/11 audit team are shown in the table below.

Table 4: **Audit team**

Name	Contact details	Responsibilities
Steve Nicklin District Auditor/ Engagement Lead	s-nicklin@audit-commission.gov.uk 0844 798 1621	Responsible for the overall delivery of the audit including the quality of outputs, signing the opinion and conclusion, and liaison with the Chief Fire Officer.
Lynn Hunt Audit Manager	l-hunt@audit-commission.gov.uk 0844 798 1675	Manages and coordinates the different elements of the audit work. Key point of contact for the Chief Finance Officer.
Chris Clancy Team Leader	c-clancy@audit-commission.gov.uk 0844 798 1647	On-site supervision of audit fieldwork and key point of contract for the Chief Accountant.

Independence and objectivity

23 I am not aware of any relationships that may affect the independence and objectivity of audit staff, which we are required by auditing and ethical standards to communicate to you.

24 I comply with the ethical standards issued by the APB and with the Commission's requirements in respect of independence and objectivity as summarised in appendix 2.

Meetings

25 The audit team will maintain knowledge of your issues to inform our risk-based audit through regular liaison with key officers. Our proposals are set out in appendix 4.

Quality of service

26 We are committed to providing you with a high quality service. If you are in any way dissatisfied, or would like to discuss how we can improve our service, please contact me in the first instance. Alternatively, you may wish to contact Mike Haworth Maiden, Lead Director for Local Government, on 0844 798 2305.

27 If we are unable to satisfy your concerns, you have the right to make a formal complaint to the Audit Commission. The complaints procedure is set out in the leaflet 'Something to Complain About' which is available from the Commission's website or on request.

Planned outputs

28 Reports will be discussed and agreed with the appropriate officers before being issued to the Governance Committee.

Table 5: **Planned outputs**

Planned output	Indicative date
Opinion audit plan	February 2011
Annual governance report	September 2011
Auditor's report giving an opinion on the financial statements	September 2011
Final accounts memorandum (If required)	October 2011

Appendix 1 Basis for fee

The Audit Commission is committed to targeting its work where it will have the greatest effect, based upon assessments of risk and performance. This means planning work to address areas of risk relevant to our audit responsibilities and reflecting this in the audit fees.

The risk assessment process starts with the identification of the significant financial and operational risks applying to the Authority with reference to:

- our cumulative knowledge of the organisation;
- planning guidance issued by the Audit Commission;
- the specific results of previous and ongoing audit work;
- interviews with officers; and
- liaison with Internal Audit.

Assumptions

In setting the fee, I have assumed that:

- you will inform us of significant developments impacting on the audit;
- Internal Audit meets appropriate professional standards and completes their planned work in sufficient time for us to place reliance on it for the purposes of our opinion audit;
- good quality working papers and records will be provided to support the financial statements by the agreed date;
- requested information will be provided within agreed timescales; and
- prompt responses will be provided to draft reports; and

Where these assumptions are not met, I will be required to undertake additional work which is likely to result in an increased audit fee.

Appendix 2 Independence and objectivity

Auditors appointed by the Audit Commission are required to comply with the Commission's Code of Audit Practice and Standing Guidance for Auditors, which defines the terms of the appointment. When auditing the financial statements, auditors are also required to comply with auditing standards and ethical standards issued by the Auditing Practices Board (APB).

The main requirements of the Code of Audit Practice, Standing Guidance for Auditors and the standards are summarised below.

International Standard on Auditing (UK and Ireland) 260 (Communication of audit matters with those charged with governance) requires that the appointed auditor:

- discloses in writing all relationships that may bear on the auditor's objectivity and independence, the related safeguards put in place to protect against these threats and the total amount of fee that the auditor has charged the client; and
- confirms in writing that the APB's ethical standards are complied with and that, in the auditor's professional judgement, they are independent and their objectivity is not compromised.

The standard defines 'those charged with governance' as 'those persons entrusted with the supervision, control and direction of an entity'. In your case, the appropriate addressee of communications from the auditor to those charged with governance is the Governance Committee. The auditor reserves the right, however, to communicate directly with the Authority on matters which are considered to be of sufficient importance.

The Commission's Code of Audit Practice has an overriding general requirement that appointed auditors carry out their work independently and objectively, and ensure that they do not act in any way that might give rise to, or could reasonably be perceived to give rise to, a conflict of interest. In particular, appointed auditors and their staff should avoid entering into any official, professional or personal relationships which may, or could reasonably be perceived to, cause them inappropriately or unjustifiably to limit the scope, extent or rigour of their work or impair the objectivity of their judgement.

The Standing Guidance for Auditors includes a number of specific rules. The key rules relevant to this audit appointment are as follows.

- Appointed auditors should not perform additional work for an audited body (ie work over and above the minimum required to meet their statutory responsibilities) if it would compromise their independence or might give rise to a reasonable perception that their independence could be compromised. Where the audited body invites the auditor to carry out risk-based work in a particular area that cannot otherwise be justified as necessary to support the auditor's opinion and conclusions, it should be clearly differentiated within the Audit and Inspection Plan as being 'additional work' and charged for separately from the normal audit fee.
- Auditors should not accept engagements that involve commenting on the performance of other auditors appointed by the Commission on Commission work without first consulting the Commission.
- The District Auditor responsible for the audit should, in all but the most exceptional circumstances, be changed at least once every five years.
- The District Auditor and senior members of the audit team are prevented from taking part in political activity on behalf of a political party, or special interest group, whose activities relate directly to the functions of local government or NHS bodies in general, or to a particular local government or NHS body.

The District Auditor and members of the audit team must abide by the Commission's policy on gifts, hospitality and entertainment.

Appendix 3 The Clarity project

Introduction

The main changes you will notice in our 2010/11 audit approach cover:

- Testing strategies;
- Related Party Transactions;
- Accounting Estimates; and
- Reporting deficiencies in internal control.

Testing strategies

ISA (UK&I) 330 (The Auditor's response to assessed risks), requires me to review all material year-end adjustment journals. I can do this by using interrogation tools such as CAATs (Computer aided audit techniques), IDea software or excel, depending on the compatibility of your general ledger software.

ISA (UK&I) 330 also requires me to undertake substantive testing on all material classes of transactions. This means that I will need to sample test income and expenditure assertions in the 2010/11 financial statements, To enable me to do this you will need to provide a full audit trail between the BVACOP service analysis and the source documentation via project codes, journal postings and feeder systems.

My audit team will discuss a suitable approach to this work with you.

Related Party Transactions

ISA (UK&I) 550 (Related parties) requires me to review your procedures for identifying related party transactions and obtain an understanding of the controls that you have established to identify such transactions. I will also review minutes and correspondence for evidence of related party transactions and carry out testing to ensure the related party transaction disclosures you make in the financial statements are complete and accurate.

Accounting Estimates

ISA (UK&I) 540 (Auditing Accounting Estimates, Including Fair Value Accounting Estimates, And Related Disclosures) requires me to look at your accounting estimates in detail. As part of my audit I will request a list of these from you. I will need to know in particular:

- the process you use to make your accounting estimates;
- the controls you use to identify them;
- whether you use an expert to help you in making the accounting estimates;

- whether any alternative estimates have been discussed and why they have been rejected;
- how you assess the degree of estimation uncertainty (this is the uncertainty arising because the estimate cannot be precise or exact); and
- the prior year's accounting estimates outcomes, and whether there has been a change in the method of calculation for the current year.

Deficiencies in internal control

ISA (UK&I) 265 (Communicating Deficiencies In Internal Control To Those Charged With Governance And Management) is a new standard.

If I identify a deficiency in any of your internal controls during the audit, I will undertake more audit testing to decide whether the deficiency is significant. If I decide the deficiency is significant, I will report it in writing to those charged with governance.

Appendix 4 Working together

Meetings

The audit team will maintain knowledge of your issues to inform our risk-based audit through regular liaison with key officers.

Our proposal for the meetings is as follows.

Table 6: **Proposed meetings with officers**

Key officers	Audit Commission staff	Timing	Purpose
Chief Fire Officer and Chief Financial Officer	District Auditor and Audit Manager (AM)	January, September and November	General update plus: ■ January – audit plan; ■ September – annual governance report; and ■ October – annual audit letter.
Chief Accountant	AM and Team Leader (TL)	Weekly during post-statement site visit Quarterly the rest of the year	Update on audit issues
Governance Committee	District Auditor and AM, with TL as appropriate	As determined by the Committee	Formal reporting of: ■ Audit Plan; ■ Annual governance report; ■ Annual Audit Letter; and ■ Other issues as appropriate.

Sustainability

The Audit Commission is committed to promoting sustainability in our working practices and we will actively consider opportunities to reduce our impact on the environment. This will include:

- reducing paper flow by encouraging you to submit documentation and working papers electronically;
- use of video and telephone conferencing for meetings as appropriate; and
- reducing travel.

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www.audit-commission.gov.uk March 2011

PREVENTING PROTECTING RESPONDING

TYNE AND WEAR FIRE AND RESCUE AUTHORITY

MEETING: 21ST MARCH 2011

SUBJECT: INTERNAL AUDIT STRATEGY AND OPERATIONAL PLAN FOR 2011/2012

REPORT OF THE HEAD OF INTERNAL AUDIT

1. Purpose of Report

1.1 To enable the Governance Committee to consider and comment on the proposed Internal Audit Strategy, and Operational Plan for 2011/2012.

2. Background

2.1 The Terms of Reference of the Committee include *'consider and endorse the Internal Audit Strategy and Operational Plan, and monitor performance'*.

2.2 The current Internal Audit Strategy was agreed on 31st March 2008. As part of the ongoing development of the service the Strategy has been reviewed and whilst, in large part, it remains fit for purpose, the audit risk assessment process has been updated to better take account of the Authority's key risk areas and Corporate Risk Profile. Therefore, the Internal Audit Strategy has been updated and is included for agreement.

3. Recommendation

3.1 The Governance Committee is invited to consider and, if appropriate, make comment on the attached proposed Internal Audit Strategy, and Operational Plan.

4. Background Papers

4.1 None

Tyne and Wear Fire and Rescue Authority

Internal Audit Strategy

1. Regulatory Framework

1.1 There are legislative requirements that relate to the provision of internal audit within fire and rescue authorities, namely:

The Local Government Act 1972 (S151) requires that *"every local authority shall make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs*".

The Accounts and Audit Regulations 2003 (as amended in 2006) specify certain requirements of local authorities. In order to comply with these regulations the Authority needs to maintain an adequate and effective system of internal audit of its accounting records, and of its system of internal control.

1.2 The responsible financial officer within the Authority is the Finance Officer and one of the ways that this responsibility is exercised is through the work of internal audit (set out in the Authority's Financial Regulations, Para 1.3.2).

2. Professional Standards and Ethics

Chartered Institute of Public Finance and Accountancy (CIPFA)

2.1 CIPFA has published a Code of Practice for Internal Audit in Local Government.

Institute of Internal Auditors - UK (IIA-UK)

2.2 The IIA-UK has produced Standards for the Professional Practice of Internal Auditing.

Ethics

2.3 The CIPFA Code of Practice for Internal Audit sets out in its introduction, minimum ethical standards for the performance and conduct of internal auditors.

2.4 The principles that must be observed are:

- integrity;
- objectivity;
- competence; and
- confidentiality.

3. Provision of Internal Audit

3.1 The Finance Officer to the Authority is the Executive Director of Commercial and Corporate Services of Sunderland City Council, who also provides financial services to the Authority, including internal audit. In considering the options for the provision of internal audit the Finance Officer has decided to maintain an in-house service (Internal Audit and Counter Fraud Unit), supplemented by external resource / expertise where required. This option provides for flexibility, a local presence, the development and retention of local knowledge of the organisation whilst ensuring the optimum use of financial resources. This option will be kept under review.

3.2 The Authority complies with the above requirements (regulatory framework, professional standards and ethics) through the operation and work of the internal audit service.

4. Role of Internal Audit

4.1 The roles and responsibilities of the internal audit service are set out in its Audit Charter which is kept under review and agreed by the Committee.

5. Quality System

5.1 The internal audit service maintains processes for planning, implementing, checking and reviewing the way in which internal audit work is delivered in line with professional standards.

6. Planning and Resources

6.1 It is important that the service keeps under review the resources required in order for it to fulfil its role in the medium to longer term. As such, as part of the annual planning process, the potential coverage of internal audit activity for the following 3 years is assessed alongside the existing resources available.

6.2 In developing the coverage of internal audit work it is appropriate to cover the key risk areas of the business over a period of years. The frequency and scope of the work is driven by an assessment of risk in consultation with key officers and a review of key documents. In order to achieve this, an audit risk assessment and planning methodology is used, as follows:

a. A list of key risk areas has been determined which covers the main areas of inherent risk to the Authority (set out at Appendix 1).

b. Each key risk area is assessed based on the strength of the control arrangements known to be in place to manage the risks in that area, the likelihood of a failure in control, and the impact that failure could have. Regard was given to the key risks set out in the Authority's Corporate

Risk Profile. This results in an assessment of the level of need for audit work in order to be able to provide an opinion on the control environment in place in relation to each key risk area for each financial year.

c. In order to complete the risk assessment as outlined above, the following is carried out:

- consultation with the Chief Fire Officer and Senior Managers to identify key issues facing the Authority nationally, regionally and locally to ensure that key risks facing the Authority are prioritised;
- consideration of new initiatives, plans, and legislation;
- discussions with the external auditor, and;
- strategic risks as identified in discussion with the Finance Officer.

d. The available audit resources are then allocated within the annual Operational Plan in accordance with the above taking into account the necessary skills and experience to undertake the work.

7. Skills and Competence

7.1 As a shared service, internal audit has a wide pool of skills and experience, including IT auditors. The head of internal audit and the section's manager are professionally qualified and all staff are trained to deliver work to professional standards.

7.2 The staffing resource available within the shared internal audit service equates to 15 full time equivalent members of staff, with qualifications as follows:

Qualified Accountants:	5
Institute of Internal Auditors - Professional Level:	5
Association of Accounting Technicians:	4
Qualification in Computer Audit:	2

A range of staff will be used in undertaking work for the Authority.

8. Performance Indicators

8.1 A range of performance indicators are maintained covering Efficiency and Effectiveness, Quality and Customer Satisfaction. Performance against these areas will be reported to the Chief Fire Officer on a quarterly basis and the Governance Committee on a 6 monthly basis.

9. Reporting

9.1 An Interim and Annual Report will be prepared in order to give assurance or otherwise to Members that they can rely on the work of internal audit.

Appendix 1

Key Risk Areas

Corporate Governance
Service / Business Planning, IRMP
Financial Management
Risk Management
Procurement and Contract Management
Human Resource Management
Asset Management
ICT
Fraud and Corruption
Information Governance
Business Continuity and Contingency Planning
Performance Management
Payroll
Partnership Working
Project Management

Tyne and Wear Fire and Rescue Authority

Internal Audit Operational Plan for 2011/2012

1. Introduction

1.1 This document sets out the proposed Internal Audit Operational Plan and key performance measures for 2011/2012.

2. Development of Internal Audit Operational Plan

2.1 In developing the coverage of internal audit work it is appropriate to cover the key risk areas of the business over a period of years. The frequency and scope of the work is driven by an assessment of risk in consultation with the Chief Fire Officer (as set out in the Internal Audit Strategy). The Operational Plan sets out the work scheduled for the next financial year.

2.2 As specific areas of concern or irregularity may require investigation as and when they arise, a contingency allowance is made for this work.

2.3 Where individual audits cannot be undertaken as originally planned (e.g. service no longer provided), attempts will be made to replace the audit with a suitable replacement in consultation with the Chief Fire Officer and Finance Officer. Where these changes are agreed this shall be considered a variation to this Plan for the purposes of performance reporting.

2.4 In addition, unforeseen work can arise due to new areas of service or increased risk which is appropriate to prompt audit work in the year. Therefore, in order to allow some flexibility, a contingency allowance is also made to enable such work to be undertaken without adversely affecting the delivery of the planned audit work.

2.5 Time has also been allocated for the provision of advice and guidance.

2.6 Within the plan, provision has also been made to carry out follow up work to monitor the implementation of previously agreed recommendations (except for low risk).

3. Planned Audit Work for 2011/2012

3.1 The following audits are planned.

3.1.1 <u>PFI Contract Management</u> (12 days)
This audit will examine the arrangements to manage and monitor the services provided by the Authority’s new PFI contractor and the accuracy of the contract payments.

3.1.2 Payroll (12 days)
Detailed checks will take place to obtain assurance on the accuracy of the Authority's payroll.

3.1.3 Project Management (15 days)
This audit will examine a key project to assess the arrangements put in place to ensure that projects are managed in an efficient and effective way.

3.1.4 Data Handling Guidelines (12 days)
The Local Government Data Handling Guidelines set out guidance for the secure and effective handling of personal information. The Fire Authority started work on implementing the Guidelines in 2010/11. This audit will review progress on implementation.

3.2 In addition to the above, 15 days have been allocated for proactive counter fraud and error work in relation to:

- Payment of allowances;
- Overtime;
- Honoraria;
- Premium rate telephone calls.

3.3 Each audit is linked to the appropriate key risk area(s) to identify the audit work that will inform the opinion in relation to each key risk area. Appendix 1 to this report shows all of the key risk areas and those audits that contribute towards the opinion on each area. It should be noted that some audits contribute towards the opinion of more than one key risk area and some key risk areas rely on a number of audits.

3.4 In addition to the above, audit work is also undertaken on the Lead Authority's key financial systems, which are used by the Authority. Systems planned to be audited during 2011/2012 include:

- Accounts Payable;
- Periodic Income;
- Payroll.

4. Reporting Protocols

4.1 At the conclusion of each individual audit a Draft Report and, if necessary, a proposed Action Plan will be forwarded to the appropriate manager. Once agreement has been reached, a Final Report (including any Action Plan) will be forwarded to the Chief Fire Officer. Where audits highlight issues which need to be brought to the attention of the Finance Officer they will be raised as and when necessary.

4.2 A quarterly progress report will be presented to the Chief Fire Officer indicating the level of achievement against agreed targets and any major findings arising from the audit work undertaken.

4.3 The Governance Committee will be updated on progress against the audit plan approximately half way through the year.

4.4 An Annual Report will be prepared for the Authority and the Governance Committee, in order to give assurance, or otherwise, to Members that they can rely on the internal control framework of the Authority.

5. Performance Management

5.1 All work undertaken will be in accordance with its policies and procedures, which are based upon the professional standards required by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Institute of Internal Auditors (IIA-UK).

5.2 The Key Performance Indicators which will be used to measure the performance of the service throughout the year, are shown in Appendix 2.

6. Variations to Audit Plan

6.1 As stated in paragraphs 2.3 and 2.4 above, in order to allow some flexibility in the work Internal Audit Services undertakes, a contingency allowance is made to enable unforeseen requests to be responded to without adversely affecting the delivery of the planned audit work. However, if the contingency allowance has been exhausted an assessment will be carried out to determine whether requests for additional work should be undertaken, based on the impact upon the delivery of the plan and the risks associated with the work requested.

Appendix 1

Detailed Audit Coverage

Key Risk Area	Internal Audit Risk Assessment (Residual Risk)	Implication for the Audit Plan	Overall Opinion from Previous 3 years work	Audits Planned 2011/12
Corporate Governance	5%	Recent audit work in this area confirmed strong arrangements in place. No specific audit work necessary.	Good	
Service / Business Planning, IRMP	6%	Recent audit work has highlighted sound arrangements in place.	Good	
Financial Management	5%	New PFI supplier in place, contract management arrangements to be reviewed.	Satisfactory	PFI Contract Management
Risk Management	8%	Recent audit work has highlighted sound arrangements in place.	Good	
Procurement and Contract Management	14%	New PFI supplier in place, contract management arrangements to be reviewed.	Satisfactory	PFI Contract Management
Human Resource Management	5%	History of good performance therefore no specific audit work required.	Good	
Asset Management	8%	Recent audit work has highlighted sound arrangements in place.	Good	
ICT	24%	A review of the progress in implementing the Data Handling guidelines will be undertaken.	Good	Data Handling Guidelines
Fraud and Corruption	2%	Consideration of counter fraud testing as the back office go through a period of change and review.	Good	
Information Governance	25%	Information governance covered in 2010/2011, information security in relation to ICT to be covered during 2011/2012.	Good	Data Handling Guidelines
Business Continuity and Contingency Planning	24%	Arrangements were in a state of change during the previous audit, follow up work to be completed.	Satisfactory	Follow up work to be completed
Performance Management	5%	Recent audit work has highlighted sound arrangements in place.	Good	
Payroll	5%	Transaction testing in to be undertaken following move to monthly pay.	Satisfactory	Payroll Testing
Partnership Working	14%	Risks in relation to this area will be reviewed in discussion with key officers of the Authority.		
Project Management	15%	Project Management arrangements to be reviewed for a key project.		Project Management Arrangements

Internal Audit and Counter Fraud Unit - Overall Objectives, Key Performance Indicators (KPI's) and Targets for 2011/2012		
Efficiency and Effectiveness		
Objectives	**KPI's**	**Targets**
1) To ensure the service provided is effective and efficient.	1) Complete sufficient audit work to provide an opinion on the key risk areas identified.	1) All key risk areas covered over a 3 year period
	2) Percentage of draft reports issued within 15 days of the end of fieldwork.	2) 90%
	3) Percentage of audits completed by the target date (from scoping meeting to issue of draft report).	3) 80%

Appendix 2

Internal Audit and Counter Fraud Unit - Overall Objectives, Key Performance Indicators (KPI's) and Targets for 2011/2012		
Quality		
Objectives	**KPI's**	**Targets**
1) To maintain an effective system of Quality Assurance.	1) Opinion of External Auditor	1) Satisfactory opinion
2) To ensure recommendations made by the service are agreed and implemented.	2) Percentage of agreed high, significant and medium risk internal audit recommendations which are implemented.	2) 100% for high and significant. 90% for medium risk
Client Satisfaction		
Objectives	**KPI's**	**Targets**
1) To ensure that clients are satisfied with the service and consider it to be good quality.	1) Results of Post Audit Questionnaires	1) Overall average score of better than 1.5 (where 1=Good and 4=Poor)
	2) Results of other Questionnaires	2) Results classed as 'Good'
	3) Number of Complaints / Compliments	3) No target – actual numbers will be reported

PREVENTING PROTECTING RESPONDING

TYNE & WEAR FIRE AND RESCUE AUTHORITY

GOVERNANCE COMMITTEE MEETING: 21ST MARCH 2011

SUBJECT: TREASURY MANAGEMENT POLICY AND STRATEGY 2011/2012, INCLUDING PRUDENTIAL 'TREASURY MANAGEMENT' INDICATORS FOR 2011/2012 TO 2013/2014

REPORT OF THE FINANCE OFFICER

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1. Introduction

1.1 The purpose of this report is to inform Governance Committee on the Treasury Management Policy and Strategy (including both borrowing and investment strategies) proposed for 2011/2012 and to note the Prudential 'Treasury Management' Indicators for 2011/2012 to 2013/2014 and to provide comments to the Authority on the proposed policy and indicators where appropriate.

2. Description of Decision

2.1 Committee is requested to:
- Provide any appropriate comments to the Authority on the proposed:
  - Annual Treasury Management Policy and Strategy (including specifically the Annual Borrowing and Investment Strategies);
  - prudential 'Treasury Management' indicators;

3. Treasury Management

3.1 Treasury management is defined as "the management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

The Treasury Management function is a specialist service that is carried out by Sunderland City Council on behalf of the Authority.

3.2 **Statutory requirements**

The Local Government Act 2003 (the Act) and supporting regulations requires the Authority to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Management Indicators for the next three years to ensure that the Authority's capital investment plans are affordable, prudent and sustainable, these are set out in Appendix 1.

The Act also requires the Authority to adopt a Treasury Management Policy Statement (detailed in Appendix 2) and to set out its Treasury Management

Strategy comprising the Authority's strategy for borrowing and the Authority's policies for managing its investments and giving priority to the security and liquidity of those investments (Appendix 3).

The Department of Communities and Local Government issued revised investment guidance which came into effect from 1 April 2010. There are no major changes required over and above the arrangements that the Authority already has in place and were included in the revised CIPFA Treasury Management Code of Practice 2009 that the Authority fully adheres to.

3.3 **CIPFA requirements**

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised November 2009) was adopted by the Authority on 22nd March 2010.

The primary requirements of the Code are as follows:

1. The Authority will create and maintain, as the cornerstones for effective treasury management:
   - a treasury management policy statement, stating the policies, objectives and approach to risk management of its treasury management activities;
   - suitable Treasury Management Practices (TMP's), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.

   The content of the policy statement (is detailed in Appendix 2) and the TMP's follow the recommendations contained in Sections 6 and 7 of the Code, subject only to amendment where necessary to reflect the particular circumstances of the Authority. Such amendments which are minor in nature do not result in the Authority deviating from the Code's key principles however.

2. The Authority will receive reports on treasury management policies, practices and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid-year review and an annual report after its close, in the form prescribed in its TMP's.

3. The Authority delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to this Committee, and for the execution and administration of treasury management decisions to the Finance Officer, who acts in accordance with the organisation's Policy Statement, TMPs and CIPFA's Standard of Professional Practice on Treasury Management.

4. The Authority has previously nominated the Governance Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

Treasury Management Strategy for 2011/2012

3.4 The Treasury Management Strategy comprises a Borrowing and an Investment Strategy. These set out the Authority's policies for managing its borrowing and investments and for giving priority to the security and liquidity of investments.

3.5 There are no major changes being proposed to the overall Treasury Management Strategy in 2011/2012 which maintains the prudent approach adopted by the Authority in previous years. Particular areas that inform the strategy include the extent of potential borrowing included in the Authority's capital programme, the availability of borrowing, and the current and forecast world and UK economic position, in particular forecasts relating to interest rates and security of investments.

3.6 The proposed Treasury Management Strategy Statement for 2011/2012 is set out in Appendix 3 and is based upon the views of the Finance Officer, supplemented with market data, market information and leading market forecasts provided by the Authority's treasury adviser, Sector Treasury Services.

3.7 The strategy is subject to regular review to ensure compliance to the agreed treasury management strategy and that the strategy adapts to changing financial markets as appropriate. It is pleasing to note that the current average rate of borrowing at 3.35% is low in comparison with other local authorities whilst the current rate earned on investments at 1.49% is higher than the overall benchmark rate. In addition debt rescheduling undertaken by the lead authority, Sunderland City Council, has achieved significant savings in interest charges and discounts and these interest savings have been secured for many years to come. For example, since November 2008 total debt has been rescheduled worth £59.5 million with an ongoing reduction in interest costs of just under £1.0 million per annum. The Authority has benefitted from this exercise to the tune of £0.278 million on average per annum, in reduced debt charges over the past 3 financial years since. Market conditions are under constant review so that the Authority can take a view on the optimum time to carry out further borrowing or debt rescheduling.

4. Suggested Reason for Decision

4.1 To comply with statutory requirements.

5. Alternative Options

5.1 No alternatives are submitted for the Authority's consideration

Background Papers

Sector City Watch (Monthly)

Local Government Act 2003

The Prudential Code for Capital Finance in Local Authorities (Fully Revised Second Edition

Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes (Fully Revised Second Edition 2009)

Treasury Management in the Public services Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (Fully Revised Third Edition)

Appendix 1

Prudential 'Treasury Management' Indicators 2011/2012 to 2013/2014

The indicators below relate to Treasury Management (all indicators relating to capital financing have been removed for clarity and can be found in the Capital Programme 2011/2012 and Treasury Management Policy and Strategy 2011/2012, including Prudential Indicators for 2011/2012 to 2013/2014 report to Authority on 28th February 2011.

P5 In respect of its external debt, it is recommended that the Authority approves the following authorised limits for its total external debt, gross of investments for the next three financial years, and agrees the continuation of the previously agreed limit for the current year since no change to this is necessary. These limits separately identify borrowing from other long-term liabilities such as PFI schemes and finance leases. The Authority is asked to approve these limits and to delegate authority to the Finance Officer, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for the authority. Any such changes made will be reported to the Authority at the next meetings following the change.

	Authorised Limit for External Debt			
	2010/2011 £000	**2011/2012 £000**	**2012/2013 £000**	**2013/2014 £000**
Borrowing	25,113	25,622	27,270	27,200
Finance Lease	62	56	50	44
Other long term liabilities	20,233	20,685	21,067	21,437
Total	**45,408**	**46,363**	**48,387**	**48,681**

The Finance Officer reports that these authorised limits are consistent with the Authority's current commitments, existing plans and the proposals in this report for capital expenditure and financing, and with its approved treasury management policy statement and practices. The Finance Officer also confirms that they are based on the estimate of most likely, prudent, but not worst case scenario, with, in addition, sufficient headroom over and above this to allow for operational management, for example unusual cash movements. Risk analysis and risk management strategies have been taken into account, as have plans for capital expenditure, estimates of the Capital Financing Requirement and estimates of cash flow requirements for all purposes.

In taking its decisions on the Revenue Budget and Capital Programme for 2011/2012, the Authority is asked to note that the authorised limit determined for 2011/2012, (see P5 above), will be the statutory limit determined under section 3(1) of the Local Government Act 2003.

P6 The Authority is also asked to approve the following operational boundary for external debt for the same time period and agrees the continuation of the previously agreed limit for the current year since no change to this is necessary. The proposed operational boundary for external debt is based on the same estimates as the authorised limit, but reflects directly the estimate of the most likely, prudent but not worst case scenario level, without the additional headroom included within the authorised limit to allow for example for unusual cash movements, and equates to the maximum of external debt projected by this estimate. The operational boundary represents a key management tool for in year monitoring. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified. The Authority is also asked to delegate authority to the Finance Officer, within the total operational boundary for any individual year, to effect movement between the separately agreed figures for borrowing and other long term liabilities, similar to the authorised limit set out above.

The operational boundary limit will be closely monitored and a report will be made to the Authority if it is exceeded at any point. In any financial year, it is generally only expected that the actual debt outstanding will approach the operational boundary when all of the long-term borrowing has been undertaken for that particular year and will only be broken temporarily as a result of the timing of debt rescheduling.

	Operational boundary for external debt			
	2010/2011	**2011/2012**	**2012/2013**	**2013/2014**
	£000	**£000**	**£000**	**£000**
Borrowing	20,113	20,622	22,270	22,200
Finance Lease	62	56	50	44
Other long term liabilities	20,233	20,685	21,067	21,437
Total	**40,408**	**41,363**	**43,387**	**43,681**

P7 The Authority's actual external debt at 31st March 2010 was £17.655 million (calculated on the basis that all Authority debt is classed as external), comprising £17.593 million borrowing and £0.062 million in respect of a finance lease.

The Authority includes an element for long-term liabilities relating to PFI schemes and finance leases in its calculation of the operational and authorised boundaries to allow further flexibility over future financing. It should be noted that actual external debt is not directly comparable to the authorised limit and operational boundary, since the actual external debt reflects the position at any one point in time and allowance needs to be made for cash flow variations.

P9 The Authority is also required to indicate if it has adopted the CIPFA Code of Practice for Treasury Management in the Public Services. This original 2001 Code was adopted on 20th November 2002 by the Fire and Rescue Authority and the revised Code was adopted on 22nd March 2010.

The objective of the Prudential Code is to provide a clear framework for local authority capital finance that will ensure for individual local authorities that:

(a) capital expenditure plans are affordable;
(b) all external borrowing and other long term liabilities are within prudent and sustainable levels;
(c) treasury management decisions are taken in accordance with professional good practice;

and that in taking decisions in relation to (a) to (c) above the local authority is

(d) accountable, by providing a clear and transparent framework.

Further, the framework established by the Code should be consistent with and support:

(e) local strategic planning;
(f) local asset management planning;
(g) proper option appraisal.

In exceptional circumstances the objective of the Code is to provide a framework that will demonstrate that there is a danger of not ensuring the above, so that the Authority can take timely remedial action.

P10 It is recommended that the upper limit total on fixed interest rate exposures is set at £105 million in 2011/2012, £125 million in 2012/2013 and £145 million in 2013/2014.

P11 It is further recommended that the upper limit total on variable interest rate exposures is set at £60 million in 2011/2012, £60 million in 2012/2013 and £50 million in 2013/2014.

P12 It is recommended that the upper and lower limits are set in total for the maturity structure of borrowings as follows:

Amount of projected borrowing that is fixed rate maturing in each period expressed as a percentage of total projected borrowing that is fixed rate at the start of the period:

	Upper limit	Lower limit
Under 12 months	50%	0%
12 months and within 24 months	60%	0%
24 months and within 5 years	80%	0%
5 years and within 10 years	100%	0%
10 years and within 20 years	100%	0%
20 years and within 30 years	100%	0%
30 years and within 40 years	100%	0%
40 years and within 50 years	100%	0%
over 50 years	100%	0%

P13 A maximum maturity limit of £100 million is set for each financial year (2011/2012, 2012/2013 and 2013/2014) for long term investments, (those over 364 days), made by the authority. This gives additional flexibility in undertaking the Treasury Management function. Should any external fund managers be appointed during the year, these limits will be apportioned accordingly. The type of investments to be allowed are detailed in the Annual Investment Strategy (Appendix 3).

Appendix 2

Treasury Management Policy Statement

In line with CIPFA recommendations, on the 22nd March 2010 the Authority adopted the following Treasury Management Policy Statement, which defines the policies and objectives of its treasury management activities:

- The Authority defines its treasury management activities as: The management of the Authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks".

- The Authority regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.

- The Authority acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

The Authority needs to re-affirm its commitment to the above Treasury Management Policy Statement each year.

Appendix 3

Treasury Management Strategy Statement for 2011/2012

1. Introduction

1.1 The Local Government Act 2003 and subsequent guidance requires the Authority to set out its Treasury Management Strategy for Borrowing and to prepare an Annual Investment Strategy. This sets out the Authority's policies for managing its investments and for giving priority to the security and liquidity of those investments.

The suggested strategy for 2011/2012 is set out below and is based upon the Finance Officer's views on interest rates, supplemented with leading market forecasts and other financial data available and advice provided by the Authority's treasury adviser, Sector Treasury Services.

1.2 The treasury management strategy covers:

A. Borrowing Policy and Strategy

- treasury limits for 2011/2012 to 2013/2014
- the past and current treasury management position
- the borrowing requirement 2011/2012
- prudential and treasury management Indicators for 2011/2012 to 2013/2014
- prospects for interest rates
- the borrowing strategy
- policy on borrowing in advance of need
- debt rescheduling

B. Annual Investment Policy and Strategy

- Investment policy and objectives
- the investment strategy
- investment types
- investments defined as capital expenditure
- investment limits
- provision for credit related losses
- creditworthiness policy
- monitoring of credit ratings
- past performance and current position
- outlook and proposed investment strategy
- external fund managers
- policy on use of external service providers

2. Borrowing Policy and Strategy

2.1 **Treasury Limits for 2011/2012 to 2013/2014**
It is a statutory duty under Section 3 of the Local Government Act 2003 and supporting regulations, for the Authority to determine and keep under review how much it can afford to borrow. The amount so determined is termed the

"Affordable Borrowing Limit". In England and Wales the Authorised Limit represents the legislative limit specified in the Act.

The Authority must have regard to the Prudential Code when setting the Authorised Limit, which essentially requires it to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future council tax is 'acceptable'.

Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion incorporate financing by both external borrowing and other forms of liability, such as credit arrangements. The Authorised Limit is set, on a rolling basis, for the forthcoming financial year and two successive financial years and details can be found in Appendix 1 of this report. The Authority is asked to approve these limits and to delegate authority to the Finance Officer, within the total limit for any individual year, to action movement between the separately agreed limits for borrowing and other long term liabilities where this would be appropriate. Any such changes made will be reported to the Authority at their next meetings following the change.

Also, the Authority is asked to approve the Operational Boundary Limits which are included in the Prudential Indicators (Appendix 1). This operational boundary represents a key management tool for in year monitoring. Within the operational boundary, figures for borrowing and other long-term liabilities are separately identified and the Authority is also asked to delegate authority to the Finance Officer, within the total operational boundary for any individual year, to action movement between the separately agreed figures for borrowing and other long-term liabilities, in a similar fashion to the authorised limit.

2.2 The Past and Current Treasury Management Position

2.2.1 Interest Rates 2010/2011

Interest rates were fairly static with only small variations during the current financial year, until the government, on 20th October 2010, following the Chancellor's announcement of the Spending Review, instructed the PWLB to increase the average interest rate on all new loans by an average of 1.00% above the Government's cost of borrowing. This unexpected change at the time saw an overall increase in all PWLB rates going forward of 0.87% making borrowing from this source both less affordable and less attractive. The table overleaf shows that the largest movement in rates was short term borrowing up to one year of 0.82% and by approximately 0.5% on all other maturity periods. Rates increased because of the government's actions but there has been a slow fall in interest rates since. This trend is starting to reverse but no significant movements are anticipated for the next financial year. This position will be carefully monitored however.

Loan Type	31st March 2010 %	31st December 2010 %	Difference %
7 Day Notice	0.30	0.40	0.10
1 Month	0.42	0.45	0.03
PWLB – 1 Year	0.83	1.65	0.82
5 Year	2.89	3.33	0.44
10 Years	4.19	4.58	0.39
25 Years	4.67	5.23	0.56
50 Years	4.70	5.16	0.46

The Bank of England Base Rate has remained at 0.50% since 5th March 2009 with little sign that it will be raised in the short term.

2.2.2 Long Term Borrowing 2010/2011

The Treasury Management Policy and Strategy Statement for 2010/2011 included a benchmark rate of 4.5% for all long-term borrowing.

The Authority's strategy for 2010/2011 is to adopt a pragmatic approach and to respond to any changing circumstances to seek to secure benefit for the Authority. In response to the Government's increase in PWLB rates across all PWLB loan periods, the Authority's benchmark rate for long-term borrowing was increased to 5.5% for the remainder of 2010/2011.

So far in 2010/2011 £30.50 million of long term borrowing has been undertaken by Sunderland City Council at an average rate of 3.31%, details of the new loans are shown below. It is pleasing to report that the replacement borrowing was made before the government unexpectedly and immediately increased borrowing rates by on average 1% across all loan duration periods on 20th October 2010, the date of the Spending Review.

Long Term PWLB Borrowing 2010/2011						
Date	Amount £m	Period (Years)	Rate %	Benchmark Rate %	Margin %	Loan Type
11/05/10	0.5	15	3.65	4.50	0.85	EIP*
25/05/10	10.0	4	1.99	4.50	2.51	Maturity
25/05/10	5.0	50	4.29	4.50	0.21	Maturity
27/07/10	5.0	11	3.75	4.50	1.25	Maturity
27/07/10	5.0	12	3.87	4.50	1.13	Maturity
01/09/10	5.0	50	3.96	4.50	0.54	Maturity
	30.5		3.31			
*This loan was taken out on behalf of Beamish Museum and is an Equal Instalment of Principal (EIP) loan						

There are currently nine market, Lender's Option / Borrower's Option (LOBO's), loans totalling £39.5 million. The lender has the option to alter the rate on these loans at set intervals and these can either be accepted at the new rate or be repaid without penalty. The following table shows the

LOBO's that were subject to a potential rollover in this financial year but have not been replaced as the option was not exercised.

Roll Over Dates	Lender	Amount £m	Rate %	Roll Over Periods
23/04/2010 and 23/10/2010	Barclays	5.0	4.50	Every 6 months (Variable Rate)
14/08/2010	Barclays	5.0	4.45	Every 3 years (Fixed Rate)
Total		10.0		

2.2.3 **Current Portfolio Position**

The treasury portfolio position for Sunderland City Council which the Fire and Rescue Authority forms part of, at 31st December 2010 comprised:

		Principal (£m)	Total (£m)	Average Rate (%)
Borrowing				
Fixed Rate Funding	PWLB	138.0		
	Market (LOBO's)	34.5		
	Other	0.4	172.9	3.86
Variable Rate Funding	PWLB	0.0		
	Market (LOBO's)	5.0		
	Temporary/ Other	31.1	36.1	0.92
Total Borrowing			209.0	3.35
Total Investments	In House		214.1	1.49
Net Position			(5.1)	

Sunderland City Council which the Fire Authority forms part of the total, currently has a difference between gross debt and net debt of £5.1 million, however this position is expected to change over the next few years as the Council and the Authority will have to manage their finances with significantly less government grant in both capital and revenue funding which could impact in the form of increased borrowing and possible temporary reductions to reserves, with the result that total borrowing could then exceed investments.

There are a number of risks and benefits associated with having both a large amount of debt whilst at the same time having a considerable amount of investments.

Benefits of having a high level of investments are;

- liquidity risk – having a large amount of investments means that the Authority is at less of a risk should money markets become restricted or borrowing less generally available, this mitigates against liquidity risk;
- interest is received on investments which helps the Authority to address its Strategic Priorities;
- the Authority has greater freedom in the timing of its borrowing as it can afford to wait until the timing is right rather than be subject to the need to borrow at a time when interest rates are not advantageous.

Risks associated with holding a high level of investments are;

- the Counterparty risk – institutions cannot repay the Authority investment placed with them;
- interest rate risk – the rate of interest earned on the investments will be less than that paid on debt, thus causing a loss to the Authority.

The Authority has mitigated these risks by formulating its Treasury Management Policy that incorporates both a Borrowing Strategy and an Annual Investment Strategy and has also taken prudent action to redeem debt early by temporarily using investments to the benefit of the Authority and saving on interest charges when opportunities have arisen.

2.3 **Borrowing Requirement 2011/2012**

The borrowing requirement for Sunderland City Council which the Fire and Rescue Authority forms part of, is as follows:

		2011/12 £m	2012/13 £m	2013/14 £m
1.	Capital Borrowing (potential)	47.7	15.0	15.0
2.	Replacement borrowing (PWLB)	0.0	5.0	5.0
3.	Replacement borrowing (Market)	0.0	0.0	0.0
4.	Market LOBO replacement (potential)	19.5	20.0	10.0
TOTAL – KNOWN (2+3)		**0.0**	**5.0**	**5.0**
TOTAL – POTENTIAL (1+4)		**67.2**	**35.0**	**25.0**

2.4 **Prudential and Treasury Management Indicators for 2011/2012 – 2013/2014**

Prudential and Treasury Indicators (as set out in Appendix 1) are a requirement of the CIPFA Prudential Code and are relevant for the purposes of setting an integrated treasury management strategy and to ensure that treasury management decisions are taken in accordance with good professional practice.

The Authority is also required to indicate if it has adopted the CIPFA Code of Practice on Treasury Management. The original 2001 Code was adopted on 20th November 2002 and the revised 2009 Code was adopted by the Authority on 22nd March 2010. The Authority also re-affirms its full adherence to the code annually (as set out in Appendix 5).

2.5 **Prospects for Interest Rates**

The Authority's treasury advisors are Sector Treasury Services and part of their service is to assist the Authority to formulate a view on interest rates. A number of current City forecasts for short term (Bank Rate) and longer fixed interest rates are set out in Appendix 4. The following gives the Sector Treasury Services Bank Rate forecast for the next 4 financial year ends (March).

- 2010/2011 0.50%
- 2011/2012 1.00%
- 2012/2013 2.25%
- 2013/2014 3.25%

There is a downside risk to these forecasts especially if recovery from the recession proves to be weaker and slower than currently expected and a short term upside risk should inflation pressures increase. A detailed view of the current economic background is contained within Appendix 5 to this report.

2.6 **Borrowing Strategy**

2.6.1 **Borrowing rates**

The Sector forecast in respect of interest rates for loans charged by the PWLB is as follows: -

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Mar-13	Mar-14
Bank rate	0.50%	0.50%	0.50%	0.75%	1.00%	2.25%	3.25%
5yr PWLB rate	3.30%	3.30%	3.40%	3.50%	3.60%	4.30%	5.00%
10yr PWLB rate	4.40%	4.40%	4.40%	4.50%	4.70%	5.10%	5.40%
25yr PWLB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.50%	5.70%
50yr PWLB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.50%	5.70%

A more detailed forecast from Sector is included in Appendix 4.

The main sensitivities of the forecast are likely to be;

- if it were felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate borrowing will be undertaken whilst interest rates are still relatively cheap.

- if it were felt that there was a significant risk of a sharp fall in long and short term rates, e.g. due to a marked increase of risks around a relapse into recession or, a risk of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

In conjunction with the Authority's treasury advisers, the Authority will monitor both the prevailing interest rates and the market forecasts.

With long-term interest rate forecasts set to remain around their current levels the Finance Officer, taking into account the advice of the Authority's treasury adviser considers a benchmark financing rate of 5.50% for any further long-term borrowing for 2011/2012 to be appropriate.

Consideration will be given to various options, including utilising some investment balances to fund the borrowing requirement in 2011/2012. The need to adapt to changing circumstances and revisions to profiling of capital expenditure is required, and flexibility needs to be retained to adapt to any changes that may occur.

The Finance Officer, taking advice from the Authority's treasury advisers will continue to monitor rates closely, and whilst implementing the borrowing strategy, will adopt a pragmatic approach in identifying the low points in the interest rate cycle at which to borrow.

2.7 Policy on borrowing in advance of need

The Authority will not borrow more than or in advance of its needs purely to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Authority can ensure the security of such funds.

In determining whether borrowing will be undertaken in advance of need the Authority will: -

- ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance of need;
- ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been fully considered;
- evaluate the economic and market factors that might influence the manner and timing of any decision to borrow;
- consider the merits of alternative forms of funding;
- consider alternative interest forecasts available and the most appropriate periods and repayment profiles to use;
- consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and other risks, and the level of such risks given the controls in place to minimise them.

2.8 Debt Rescheduling

The reasons for any rescheduling of debt will include:

- the generation of cash savings at minimum risk;
- in order to help fulfil the Treasury Management Strategy; and
- in order to enhance the balance of the long-term portfolio (by amending the maturity profile and/or the balance of volatility).

In previous years, debt rescheduling has achieved significant savings in interest charges and discounts and these interest savings have been secured for many years to come. For example, since November 2008 the lead authority has rescheduled debt worth £59.5 million with an ongoing reduction in interest costs of just under £1.0 million per annum. The introduction by the PWLB in 2007 of a spread between the rates applied to new borrowing and repayment of debt, which has now been compounded since 20 October 2010 by a considerable further widening of the difference between new borrowing and repayment rates, has meant that PWLB debt restructuring is much less attractive than it was before both of these measures were introduced. Consideration will also be given to other options where interest savings may be achievable by using LOBO (Lenders Option Borrowers Option) loans, and / or other market loans, in rescheduling exercises rather than solely using PWLB borrowing as the source of replacement financing but this would only be the case where this would represent best value to the Authority.

The latest interest rate projections for 2011/2012 show short term borrowing rates will be considerably cheaper than longer term rates and as such there may be potential for some opportunities to generate savings by switching from long term debt to short-term debt. However, these savings will need to be considered in the light of the size of premiums incurred, their short term nature, and the likely cost of refinancing those short term loans, once they mature, compared to the current rates of longer term debt in the existing debt portfolio.

The Authority is keeping a watching brief on market conditions in order to secure further debt rescheduling when, and if, appropriate opportunities arise. The timing of all borrowing and investment decisions inevitably includes an element of risk, as those decisions are based upon expectations of future interest rates. The policy to date has been very firmly one of risk spread and this prudent policy will be continued.

Any rescheduling undertaken will be reported to the Authority, as part of the agreed treasury management reporting procedure.

3. Annual Investment Policy and Strategy

3.1 Investment Policy and Objectives

When considering its investment policy and objectives, the Authority has taken regard to the Department of Communities and Local Government's (DCLG) Guidance on Local Government Investments ("the Guidance") and the 2009 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

The Authority's investment objectives are: -

(a) the security of capital, and
(b) the liquidity of its investments.

The Authority also aims to achieve the optimum return on its investments but commensurate with proper levels of security and liquidity. The risk appetite of the Authority is regarded as low in order to give priority to security of its investments.

The borrowing of monies purely to invest or on-lend and make a return is unlawful and the Authority will not engage in such activity.

3.2 Investment Strategy

This Strategy sets out:

- the procedures for determining the use of each class of investment (advantages and associated risk), particularly if the investment falls under the category of "non-specified investments";
- the maximum periods for which funds may be prudently committed in each class of investment;
- the amount or percentage limit to be invested in each class of investment;
- whether the investment instrument is to be used by the lead authority's in-house officers and/or by the appointed external fund managers, (if used); and, if non-specified investments are to be used in-house, whether prior professional advice is to be sought from the Authority's treasury advisers;
- the minimum amount to be held in short-term investments (i.e. an investment which the Authority may require to be repaid or redeemed within 12 months of making the investment).

3.3 Investment Types

The Authority is allowed to invest in two types of investment, namely Specified Investments and Non-specified Investments.

Specified Investments are those investments that are for a period of less than one year, are not classed as capital expenditure, and are placed with high credit rated counterparties.

Non-specified Investments are any investments which are not classified as specified investments. As the Authority only uses high credit rated counterparties this means in effect that any investments placed with those counterparties for a period of one year or more will be classed as Non-specified Investments. The Authority will not invest in any type of investment that will be classed as capital expenditure (see 3.4 below).

The type of investments to be used by the in-house team will be limited to term deposits, interest bearing accounts, and Money Market Funds and will follow the criteria as set out in Appendix 6.

3.4 **Investments Defined as Capital Expenditure**

The acquisition of share capital or loan capital in any body corporate is defined as capital expenditure under Section 16(2) of the Local Government Act 2003. Such investments have to be funded out of capital or revenue resources and are classified as 'non-specified investments'.

A loan or grant by this Authority to another body for capital expenditure by that body is also deemed by regulation to be capital expenditure by the Authority. It is therefore important for the Authority to clearly identify if the loan has been made for policy reasons or if it is an investment for treasury management purposes. The latter will be governed by the framework set by the Authority for 'specified' and 'non-specified' investments.

The Authority will not use (or allow any external fund managers it may appoint to use) any investment which will be deemed as capital expenditure.

3.5 **Investment Limits**

One of the recommendations of the Code is that local authorities should set limits for the amounts of investments that can be placed with institutions by country, sector and group. These limits are applied in the lead authority's Counterparty criteria set out in Appendix 6.

The minimum amount of overall investments that the will be held in short-term investments (less than one year) is £50 million. As the lead authority has decided to restrict most of its investments to term deposits, it will maintain liquidity by having a minimum of 30% of these short-term investments maturing within 6 months.

A maximum limit of £100 million is to be set for in-house non-specified investments over 364 days up to a maximum period of 2 years. This amount has been calculated by reference to the total cash flows available and projected, including the potential use of earmarked reserves. The Finance Officer will monitor long-term investment rates and identify any investment opportunities if market conditions change.

3.6 **Provisions for Credit Related Losses**

If any of the investments appear at risk of loss due to default, (i.e. a credit-related loss, and not one resulting from a fall in price due to movements in interest rates), then the Council will make revenue provision of an appropriate amount in accordance with proper accounting practice or any prevailing government regulations, if applicable. This position has not occurred and the lead authority mitigates this risk with its prudent investment policy.

3.7 **Creditworthiness policy**

The creditworthiness policy adopted by the lead authority takes into account not only the credit ratings issued by all three credit rating agencies (Fitch, Moody's and Standard & Poor's), but also, available market data and intelligence, the level of government support to financial institutions and advice from its Treasury Management advisors.

Set out in Appendix 6 is the detailed criteria that will be used, subject to approval, in determining the level of investments that can be invested with each counterparty or institution. Where a counterparty is rated differently by any of the 3 rating agencies, the lowest rating will be used to determine the level of investment.

3.8 **Monitoring of Credit Ratings**

- All credit ratings are monitored on a daily basis. The Authority has access to all three credit ratings agencies and is alerted to changes through its use of the Sector Treasury Services credit worthiness service.

- If a counterparty's rating is downgraded with the result that it no longer meets the Authority's minimum criteria, the Authority will cease to place funds with that counterparty. The Authority will also immediately inform its external fund manager(s), if used, to cease placing funds with that counterparty.

- If a counterparty's rating is downgraded with the result that, their rating is still sufficient for the counterparty to remain on the Approved Lending List, then the counterparty's authorised investment limit will be reviewed accordingly. A downgraded credit rating may result in the lowering of the counterparty's investment limit and vice versa. The Authority will also immediately inform its external fund manager(s), if used, of any such change(s).

Should fund managers be employed by the Authority, the Authority will establish with its fund manager(s) their credit criteria and the frequency of their monitoring of credit ratings so as to be satisfied as to their adherence to the Authority's policy.

3.9 **Past Performance and Current Position**

During 2010/2011 the Authority did not employ any external fund managers, all funds being managed by the in-house team. The performance of the fund managed by Sunderland City Council's in-house team is shown below and compares this with the relevant benchmarks and performance from the previous year:

	2009/10 Return %	**2009/10 Benchmark %**	**2010/11 Return % Year to date**	**2010/11 Benchmark % Year to date**
Performance	0.36	0.36	0.80	0.34

During 2010/2011 the Authority continues to review the optimum arrangements for the investment of its funds whilst fully observing the investment strategy in place.

3.10 **Outlook and Proposed Investment Strategy**

Based on its cash flow forecasts, the Authority together with the City Council anticipates its fund balances in 2011/2012 are likely to range between £150 million and £300 million. This represents a cautious approach and provides for funding being received in excess of the level budgeted for, and also for unexpected and unplanned levels of capital underspending in the year or re-profiling of spend into future years. In 2011/2012, with short-term interest rates forecast to be materially below long-term rates, it is possible that some investment balances may be used to fund some long-term borrowing or used for debt rescheduling. Such funding is wholly dependent upon market conditions and will be assessed and reported to the Authority if and when the appropriate conditions arise.

The Authority is not committed to any investments, which are due to commence in 2011/2012, (i.e. it has not agreed any forward deals).

Activities likely to have a significant effect on investment balances are:

- Capital expenditure during the financial year, (dependent upon timing), will affect cash flow and short term investment balances;
- Any re-profiling of capital expenditure from, and to, other financial years will also affect cash flow, (no re-profiling has been taken into account in current estimates);
- Any unexpected capital receipts or income;
- Timing of new long-term borrowing to fund capital expenditure;
- Possible funding of long-term borrowing from investment balances (dependent upon appropriate market conditions).

The Finance Officer, in conjunction with the Authority's treasury adviser Sector Treasury Services, and taking into account the minimum amount to be maintained in short-term investments, will continue to monitor investment rates closely and to identify any appropriate investment opportunities that may arise.

It is proposed that delegated authority continues to be given to the Finance Officer to vary the Lending List Criteria and Lending List itself should circumstances dictate, on the basis that changes be reported to the Authority retrospectively, in accordance with normal Treasury Management reporting procedures.

At the end of the financial year, the Authority will report on its investment activity as part of its Annual Treasury Report.

3.11 **External fund managers**

At present the lead authority does not use external fund managers.

Should this position arise in the future then the lead authority will appoint the external fund manager/s and they will have to agree to strict investment limits and investment criteria. These external fund managers will work to the following parameters:

- The institutions on the Approved Lending list of the external manager must correspond to those agreed with lead authority (i.e. only institutions on the Approved Lending List to be included as shown in Appendix 7);
- they will be allowed to invest in term deposits, Certificates of Deposit (CD's) and government gilt securities;
- An investment limit of £3 million per institution (per manager);
- A maximum limit of 50% fund exposure to government gilts;
- A maximum proportion of the fund invested in instruments carrying rates of interest for periods longer than 364 days shall not exceed 50%. Again, it is proposed to only recommend the use of fixed term deposits up to a maximum of 2 years.

3.12 **Policy on the use of external service providers**

The Authority uses Sector as its external treasury management advisers. The Authority recognises that responsibility for treasury management decisions remains with the Authority at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Authority will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subject to regular review.

4. **Scheme of delegation**

4.1 The Treasury Management Strategy Statement has been prepared in accordance with the revised Code. Accordingly, the Authority's Treasury Management Strategy (TMS) is approved annually by the Authority and the Authority now receive, as a minimum, a mid-year TMS report and an annual Treasury Management outturn report for the previous year by no later than the 30th September of the following year. In addition quarterly reports are made to the Authority and the Governance Committee and monitoring reports are reviewed by members in both executive and scrutiny functions respectively. The aim of these reporting arrangements is to ensure 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.

The Authority adopted the following reporting arrangements in accordance with the requirements of the Code: -

Area of Responsibility	Authority/ Committee/ Officer	Frequency
Treasury Management Policy Statement (revised)	Full Authority	Adoption of the new code for 2010/2011 and then as required
Treasury Management Strategy / Annual Investment Strategy	Full Authority	Annually before the start of the year
Treasury Management Strategy / Annual Investment Strategy – mid year report	Full Authority	Mid year
Treasury Management Strategy / Annual Investment Strategy – updates or revisions at other times	Full Authority	As appropriate
Annual Treasury Management Outturn Report	Full Authority	Annually by 30/9 after the end of the financial year
Treasury Management Monitoring Reports	Finance Officer	Monthly
Treasury Management Practices	Finance Officer	Annually
Scrutiny of Treasury Management Strategy	Governance Committee	Annually before Full Authority
Scrutiny of Treasury Management Performance	Governance Committee	Quarterly

5. The Treasury Management Role of the Section 151 Officer

5.1 The Finance Officer is the Authority's Section 151 Officer and has specific delegated responsibility in the Authority's Constitution to manage the borrowing, financing, and investment requirements of the Authority in accordance with the Treasury Management Policy agreed by the Authority. This includes;

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

Appendix 4

Interest Rate Forecasts

Introduction

The data below shows a variety of forecasts published by a number of institutions. The first three are individual forecasts from Sector Treasury Services, Capital Economics (an independent forecasting consultancy) and UBS (which represents summarised figures drawn from the population of all major City banks and academic institutions).

The forecast within this strategy statement has been drawn from these diverse sources and officers' own views.

1. Individual Forecasts

Sector:

Interest rate forecast – 6.1.11

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13	Mar-14
Bank rate	0.50%	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.25%	2.75%	3.00%	3.25%	3.25%
3 month LIBID	0.60%	0.70%	0.80%	1.00%	1.25%	1.50%	1.75%	2.00%	2.50%	3.00%	3.25%	3.50%	3.50%
6 month LIBID	0.90%	1.00%	1.10%	1.20%	1.50%	1.80%	2.10%	2.40%	2.80%	3.20%	3.50%	3.80%	4.00%
12 month LIBID	1.40%	1.50%	1.60%	1.80%	2.10%	2.40%	2.70%	3.00%	3.20%	3.40%	3.65%	4.00%	4.20%
5yr PWLB rate	3.30%	3.30%	3.40%	3.50%	3.60%	3.80%	3.90%	4.10%	4.30%	4.60%	4.80%	4.90%	5.00%
10yr PWLB rate	4.40%	4.40%	4.40%	4.50%	4.70%	4.80%	4.90%	5.00%	5.10%	5.20%	5.30%	5.40%	5.40%
25yr PWLB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.40%	5.40%	5.40%	5.50%	5.50%	5.60%	5.70%	5.70%
50yr PWLB rate	5.20%	5.20%	5.20%	5.30%	5.30%	5.40%	5.40%	5.40%	5.50%	5.50%	5.60%	5.70%	5.70%

Capital Economics:

Interest rate forecast – 12.1.11

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12	Mar-13	Jun-13	Sep-13	Dec-13
Bank Rate	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.50%	0.75%	1.00%	1.50%	2.00%
5yr PWLB rate	3.20%	3.20%	3.00%	2.75%	2.75%	2.90%	3.00%	3.20%	3.40%	3.60%	3.90%	4.20%
10yr PWLB rate	4.75%	4.75%	4.25%	3.75%	3.75%	3.75%	3.75%	3.75%	3.90%	4.00%	4.30%	4.60%
25yr PWLB rate	5.25%	5.25%	4.85%	4.65%	4.65%	4.65%	4.65%	4.65%	4.75%	4.85%	5.10%	5.30%
50yr PWLB rate	5.30%	5.30%	5.20%	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%	5.10%	5.20%	5.30%

UBS:
Interest rate forecast (for quarter ends) – 6.1.11

	Mar-11	Jun-11	Sep-11	Dec-11	Mar-12	Jun-12	Sep-12	Dec-12
Bank rate	0.50%	0.50%	0.75%	1.00%	1.25%	1.50%	1.75%	2.00%
10yr PWLB rate	4.30%	4.40%	4.50%	4.60%	4.70%	4.80%	4.90%	5.00%
25yr PWLB rate	5.25%	5.30%	5.35%	5.40%	5.45%	5.50%	5.55%	5.60%
50yr PWLB rate	5.35%	5.40%	5.45%	5.50%	5.55%	5.60%	5.65%	5.70%

2. Survey of Economic Forecasts

HM Treasury January 2011
The current Q4 2010 and 2011 forecasts are based on the January 2011 report. Forecasts for 2010 – 2014 are based on 32 forecasts in the last quarterly forecast – in November 2010.

BANK RATE FORECASTS		quarter ended		annual average Bank Rate			
	actual	Q4 2011		ave. 2011	ave. 2012	ave. 2013	ave. 2014
Median	0.50%	1.00%		0.90%	1.60%	2.40%	3.00%
Highest	0.50%	1.60%		2.10%	3.10%	3.60%	4.50%
Lowest	0.50%	0.50%		0.50%	0.50%	0.60%	1.20%

Appendix 5

Economic Background

1.1. Global economy

The economic downturn that began following the global credit crunch of August 2007 has continued into 2011. The sovereign debt crisis peaked in May 2010 prompted by major concerns over the size of the Greek government's total debt and annual deficit. Any default or write down of Greek debt would have a substantial impact on other countries, in particular, Portugal, Spain and Ireland. This crisis culminated in the EU and IMF putting together a €750bn support package in mid May. A second crisis, this time over Ireland in November 2010, culminated in Ireland also having to take EU support. There is a concern that Portugal will also shortly need to take EU support. That, in turn, would then cause further major concerns as to whether the current size of the support package facility put together by the EU and IMF would be big enough to cope with any crisis involving another major economy.

The unexpectedly high rate of growth in quarters 2 and 3 of 2010 in the UK and the Euro zone in Q2 were driven by strong growth in the construction sector catching up from inclement weather earlier in the year and by other short term factors. General expectations are for low (but not negative) growth in 2011 in the western economies.

1.2 UK economy

Following the general election in May 2010, the coalition government has put in place austerity measures to carry out a 'correction' of the public sector deficit over the next five years. The result of fiscal contraction will be major job losses during this period, in particular, in public sector services. This will have a knock-on effect on consumer and business confidence and appears to have also hit the housing market as house prices started on a negative trend during the summer and autumn of 2010. Mortgage approvals are also at very weak levels and are declining, all of which indicates that the housing market is likely to be very weak in 2011.

Economic Growth – GDP growth is likely to have peaked in the current period of recovery at 1.2% in quarter 2 of 2010. Growth in quarter 3 at +0.7% was also unexpectedly high. However, the outlook is for low growth in 2011/2012 although the Bank of England and the Office for Budget Responsibility are forecasting near trend growth (2.5%) i.e. above what most forecasters are currently expecting.

Unemployment – the trend of falling unemployment (on the benefit claimant count) has been replaced since July 2010 with small increases which are likely to be the start of a new trend for some years ahead of rising unemployment.

Inflation and Bank Rate – CPI has remained high during 2010. It peaked at 3.7% in April gradually declined to 3.1% in September but has now returned to the level of 3.7% in December (RPI 4.7%). Although inflation has remained above the MPC's 2% target, the MPC is confident that inflation will fall back under the target over the next two years.

The Bank of England finished its programme of quantitative easing (QE) with a total of £200bn in November 2009. However, expectations that there could be a second round of quantitative easing in early 2011, to help support economic growth, have evaporated after the surprises of the Q3 GDP figure of +0.7% and the outcome of the November Inflation Report revising the forecast for short-term inflation sharply upwards.

Sector's view is that there is unlikely to be any increase in the Bank Base Rate until the end of 2011.

AAA rating – prior to the general election, credit rating agencies had issued repeated warnings that unless there was a major fiscal contraction, then the AAA sovereign rating was at significant risk of being downgraded. Sterling was also under major pressure during the first half of the year. However, after the Chancellor's Emergency Budget on 22nd June 2010, Sterling strengthened against the US dollar and confidence has returned that the UK will retain its AAA rating. In addition, international investors now view UK government gilts as being a safe haven from EU government debt. The consequent increase in demand for gilts helped to add downward pressure on gilt yields and PWLB rates.

1.3 Economic Forecast

It is currently difficult to have confidence as to exactly how strong the UK economic recovery is likely to be, and there are a range of views in the market. Sector Treasury Services has adopted a moderate view. There are huge uncertainties in all forecasts due to the major difficulties of forecasting the following areas:

- the speed of economic recovery in our major trading partners - the US and EU
- the danger of a currency war and a resort to protectionism and tariff barriers if China does not address the issue of its huge trade surplus due to its undervalued currency
- the degree to which government austerity programmes will dampen economic growth and undermine consumer confidence
- changes in the consumer savings ratio
- the speed of rebalancing of the UK economy towards exporting and substituting imports
- the potential for more quantitative easing, and the timing of this in both the UK and US, and its subsequent reversal
- the speed of recovery of banks' profitability and balance sheet imbalances and the consequent implications for the availability of credit to borrowers
- the potential for a major EU sovereign debt crisis which could have a significant impact on financial markets and the global and UK economy

The overall balance of risks is weighted to the downside and there is some risk of a double dip recession, creating a downward spiral of falling demand, falling jobs and falling prices, although this is currently viewed as being a small risk. Sector believes that the longer run trend is for gilt yields and PWLB rates to rise due to the high volume of gilt issuance in the UK, and the high volume of debt issuance in other major western countries.

Lending List Criteria **Appendix 6**

Counterparty Criteria

The lead Authority takes into account not only the individual institution's credit ratings issued by all three credit rating agencies (Fitch, Moody's and Standard & Poor's), but also all available market data and intelligence, the level of government support and advice from its Treasury Management advisors.

Set out below are the criteria to be used in determining the level of funds that can be invested with each institution. Where an institution is rated differently by the rating agencies, the lowest rating will determine the level of investment.

Fitch / S&P's Long Term Rating	Fitch Short Term Rating	S&P's Short Term Rating	Moody's Long Term Rating	Moody's Short Term Rating	Maximum Deposit £m	Maximum Duration
AAA	F1+	A1+	Aaa	P-1	50	2 Years
AA+	F1+	A1+	Aa1	P-1	50	2 Years
AA	F1+	A1+	Aa2	P-1	40	364 days
AA-	F1+ / F1	A1+ / A-1	Aa3	P-1	20	364 days
A+	F1	A-1	A1	P-1	10	364 days
A	F1 / F2	A-1 / A-2	A2	P-1 / P-2	10	364 days
A-	F1 / F2	A-2	A3	P-1 / P-2	5	6 months
Local Authorities (limit for each local authority)					30	364 Days
Money Market Funds Maximum amount to be invested in Money Market Funds is £50 million with a maximum of £30 million in any one fund.					50	2 Years

Where the UK Government holds a shareholding in an institution the UK Government's credit rating of AAA will be applied to that institution to determine the amount the Authority can place with that institution.

Where any banks / building societies are part of the UK Government's Credit Guarantee scheme (marked with * in the Approved Lending List), these counterparties will have an AA rating applied to them thus giving them a credit limit of £40 million for a maximum period of 364 days

The Code of Practice for Treasury Management in the Public Services recommends that consideration should also be given to country, sector, and group limits in addition to the individual limits set out above, these new limits are as follows:

Appendix 6 (continued)

Country Limit
It is proposed that only countries with a minimum sovereign credit rating of AA+ by all three rating agencies will be considered for inclusion on the Approved Lending List.

It is also proposed to set a total limit of £40 million which can be invested in other countries provided they meet the above criteria. A separate limit of £300 million will be applied to the United Kingdom and is based on the fact that the government has done and is willing to take action to protect the UK banking system.

Country	Limit £m
UK	300
Non UK	40

Sector Limit
The Code recommends a limit be set for each sector in which the Authority can place investments. These limits are set out below:

Sector	Limit £m
Central Government	300
Local Government	300
UK Banks	300
UK Building Societies	150
Foreign Banks	40

Group Limit
Where institutions are part of a group of companies e.g. Lloyds Banking Group, Santander and RBS, then total limit of investments that can be placed with that group of companies will be determined by the highest credit rating of a counterparty within that group, unless the government rating has been applied. This will apply provided that:

- the government's guarantee scheme is still in place;
- the UK continues to have a sovereign credit rating of AAA; and
- that market intelligence and professional advice is taken into account.

Proposed group limits are set out in Appendix 7

Approved Lending List **Appendix 7**

	Fitch				Moody's			Standard & Poor's			
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term	Limit £m	Max Deposit Period
UK	AAA	F1+			Aaa			AAA		300	364 days
Lloyds Banking Group (see Note 1)										**Group Limit 50**	
Lloyds Banking Group plc	AA-	F1+	C	1	Aa3	-	-	A	A-1	50	364 days
Lloyds TSB Bank Plc	AA-	F1+	C	1	Aa3	P-1	C-	A+	A-1	50	364 days
Bank of Scotland Plc	AA-	F1+	C	1	Aa3	P-1	D+	A+	A-1	50	364 days
Royal Bank of Scotland Group (See Note 1)										**Group Limit 50**	
Royal Bank of Scotland Group plc	AA-	F1+	C/D	1	A1	P-1	-	A	A-1	50	364 days
The Royal Bank of Scotland Plc	AA-	F1+	C/D	1	Aa3	P-1	C-	A+	A-1	50	364 days
National Westminster Bank Plc	AA-	F1+	-	1	Aa3	P-1	C-	A+	A-1	50	364 days
Ulster Bank Ltd	A+	F1+	E	1	A2	P-1	D-	A	A-1	50	364 days
Santander Group *										**Group Limit 40**	
Santander UK plc	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	40	364 days
Cater Allen	AA-	F1+	B	1	Aa3	P-1	C-	AA	A-1+	40	364 days
Barclays Bank plc *	AA-	F1+	B	1	Aa3	P-1	C	AA-	A-1+	40	364 days
HSBC Bank plc *	AA	F1+	B	1	Aa2	P-1	C+	AA	A-1+	40	364 days

Appendix 7(continued)

	Fitch				Moody's			Standard & Poor's			
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strength	L Term	S Term	Limit £m	Max Deposit Period
Nationwide BS *	AA-	F1+	B	1	Aa3	P-1	C-	A+	A-1	40	364 days
Standard Chartered Bank *	AA-	F1+	B	1	A2	P-1	C+	A+	A-1	40	364 days
Clydesdale Bank / Yorkshire Bank **	AA-	F1+	C	1	A1	P-1	C-	A+	A-1	10	364 days
Co-Operative Bank Plc	A-	F2	B/C	3	A2	P-1	D+	-	-	5	6 months
Northern Rock ***	BBB+	F2	C	2	-	-	-	A-	A-2	0	
Top 10 Building Societies (by asset value)											
Nationwide BS (see above)											
Yorkshire BS	A-	F2	B/C	5	Baa1	P-2	D+	A-	A-2	0	
Coventry BS	A	F1	B	5	A3	P-2	C-	-	-	5	6 Months
Skipton BS	A-	F2	B/C	5	Baa1	P-2	D+	-	-	0	
Leeds BS	A	F1	B/C	5	A2	P-1	C+	-	-	10	364 Days
West Bromwich BS ***	BBB-	F3	C/D	5	Baa3	P-3	E+	-	-	0	
Principality BS ***	BBB+	F2	C	5	Baa2	P-2	D-	-	-	0	
Newcastle BS ***	BBB-	F3	C/D	5	Baa2	P-2	D-	-	-	0	
Norwich and Peterborough BS ***	BBB+	F2	C	5	Baa2	P-2	D	-	-	0	
Nottingham BS	-	-	-	-	A3	P-2	C-	-	-	5	6 Months
Foreign Banks have a combined total limit of £40m											
Australia	AA+	-	-	-	Aaa	-	-	AAA		40	364 Days
National Australia Bank	AA	F1+	B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Australia and New Zealand Banking Group Ltd	AA-	F1+	B	1	Aa1	P-1	B	AA	A-1+	20	364 Days

Appendix 7 (continued)

	Fitch				Moody's			Standard & Poor's			
	L Term	S Term	Individual	Support	L Term	S Term	Fin Strengt	L Term	S Term	Limit £m	Max Deposit Period
Commonwealth Bank of Australia	AA	F1+	A/B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Westpac Banking Corporation	AA	F1+	A/B	1	Aa1	P-1	B	AA	A-1+	40	364 Days
Canada	**AAA**				**Aaa**			**AAA**		40	364 Days
Bank of Nova Scotia	AA-	F1+	B	1	Aa1	P-1	B	AA-	A-1+	20	364 Days
Royal Bank of Canada	AA	F1+	A/B	1	Aa1	P-1	B+	AA-	A-1+	20	364 Days
Toronto Dominion Bank	AA-	F1+	B	1	Aaa	P-1	B+	AA-	A-1+	20	364 Days
Money Market Funds										50	2 Years
Prime Rate Stirling Liquidity	AAA MMF							AAAm		30	2 Years
Insight Liquidity Fund					AAA MR1			AAAm		30	2 Years
Ignis Sterling Liquidity	AAA MMF							AAAm		30	2 Years

Notes

Note 1 — **Nationalised / Part Nationalised**
The counterparties in this section will have the UK Government's AAA rating applied to them thus giving them a revised credit limit of £50 million for a maximum period of 364 days

* — Banks / Building Societies which are part of the UK Government's Credit Guarantee scheme
The counterparties in this section will have an AA rating applied to them thus giving them a revised credit limit of £40 million for a maximum period of 364 days

** — The Clydesdale Bank (under the UK section) is owned by National Australia Bank

*** — These will be revisited and used only if they meet the minimum criteria (ratings of A- and above)

Any bank which is incorporated in the United Kingdom and controlled by the FSA is classed as a UK bank for the purposes of the Approved Lending List.