City of BRADFORD
METROPOLITAN DISTRICT COUNCIL

# Minutes of a meeting of the Governance and Audit Committee held on Thursday, 14 March 2019 in Committee Room 1 - City Hall, Bradford

Commenced 10.20 am
Concluded 11.30 am

**Present – Councillors**

| LABOUR | CONSERVATIVE | LIBERAL DEMOCRAT |
|---|---|---|
| **Johnson**<br>**Thornton**<br>**Swallow** | **M Pollard** | **J Sunderland** |

**Councillor Johnson in the Chair**

**51. DISCLOSURES OF INTEREST**

In the interest of transparency all those who were Members of the West Yorkshire Pension Fund disclosed an interest.

Action: City Solicitor

**52. MINUTES**

**Resolved-**

**That the minutes of the meeting held on 24 January 2019 be signed as a correct record.**

**53. INSPECTION OF REPORTS AND BACKGROUND PAPERS**

There were no appeals submitted by the public to review decisions to restrict documents.

## 54. AUDIT STRATEGY MEMORANDUM 2018/19 - CITY OF BRADFORD METROPOLITAN DISTRICT COUNCIL

The External Auditor submitted the Audit Strategy Memorandum **(Document "AI")** which set out the audit plan for 2018/19. The document:

- described the approach to the audit of the Council's financial statements;
- included the assessment of the significant risks of material misstatement in the financial statements; and
- outlined the proposed testing strategy to address the identified risks.

It was reported that External Audit had also identified significant risks of material misstatement relating to:

- management override of controls – which was common to all entities subject to audit.
- The high degree of estimation uncertainty relating to the valuation of:
  - property, plant and equipment; and
  - pension liabilities

The Audit Strategy Memorandum also set out the approach to the Value for Money work, sufficient to enable External Audit to form a conclusion as to whether the Council had made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

It was reported that External Audit will report the findings in relation to the risks outlined to the July meeting of the Committee through the Audit Completion Report.

In response to a Member's question it was reported that the valuation of the Local Government Pension Scheme relied on a number of assumptions, most notably around the actuarial assumptions, and actuarial methodology which resulted in the Council's overall valuation. There were financial assumptions and demographic assumptions used in the calculation of the Council's valuation, such as the discount rate, inflation rates and mortality rates.

**Resolved-**

**That the Committee considered and approved the Audit Strategy Memorandum for the City of Bradford Metropolitan District Council for 2018/19.**

**Action: External Auditor**

## 55. EXTERNAL AUDIT PROGRESS REPORT

The External Auditor submitted **Document "AJ"** which updated the Committee on progress with the 2018/19 audit and highlighted key emerging national issues which may be of interest to the Committee.

It was reported that overall the audit work was on track and there were no significant issues arising from the work to date that needed to be reported to the Committee.

Members were informed that details of the work completed and on-going since the last Committee meeting included:

- Documenting systems and controls.
- Walkthroughs of the key systems.
- Updating the IT risk assessment.
- Controls testing, including general and application IT controls.
- Early substantive testing of transactions (including income and expenditure, payroll, journals and property, plant and equipment); and
- Updating the Value For Money risk assessment and early work in response to the significant VFM risks identified within the Audit Strategy Memorandum ie delivering financial sustainability over the medium term and Ofsted's inspection of Children's Social Care Services.

It was reported that in addition External Audit continued to liaise with Senior Officers, considered key agendas and papers and liaised with Internal Auditors to share knowledge and ensure that there was no duplication.

**Resolved-**

**That the Committee noted and considered the External Audit Progress report (Document "AJ").**

**Action: External Auditor**

## 56. WEST YORKSHIRE PENSION FUND AUDIT STRATEGY MEMORANDUM 2018/19

The External Auditor submitted **Document "AK"** which set out the plan for the external audit of the West Yorkshire Pension Fund for the year ended 31 March 2019.

It was reported that the document:

- described External Audit's approach to the audit of the Pension Fund's financial statements;
- included External Audit's assessment of the significant risks of material misstatement in the financial statements; and
- outlined the proposed testing strategy to address the identified risks.

External Audit had identified significant risks of material misstatement relating to:

- management override of controls, which was common to all entities subject to audit; and
- the high degree of estimation uncertainty relating to the valuation of unquoted investments.

Members were informed that External Audit would report their findings in relation to the risks outlined to the July meeting of the Committee through the Audit Completion Report.

In response to a Member's question it was reported that in relation to the risk in relation to Management override of controls detailed in Section 4 of the report that Management at various levels within an organisation were in a unique position to perpetrate fraud because of their ability to manipulate accounting records and prepared fraudulent financial statements by overriding controls that otherwise appeared to be operating effectively, Due to the unpredictable way in which such override could occur there was a risk of material misstatements due to fraud on all audits.

It was reported that in relation to the risk relating to the valuation of unquoted investments, the values included in the accounts were those provided by fund managers which were based on Net Asset Value or capital statements. This resulted in an increased risk of material misstatements.

In response to a Member's question it was reported that External Audit set a level of triviality for individual errors identified (a reporting threshold) for reporting to the Committee. Based on External Audit's preliminary assessment of overall materiality, External Audits proposed triviality threshold of £4m. If the total errors identified amounted to £4m they would be reported to the Committee.

**Resolved-**

**That the Committee considered and approved the Audit Strategy Memorandum for the West Yorkshire Pension Fund for 2018/19.**

**Action: External Auditor**

## 57. MINUTES OF WEST YORKSHIRE PENSION FUND (WYPF) JOINT ADVISORY GROUP HELD ON 31 JANUARY 2019

The Council's Financial Regulations required the minutes of meetings of the WYPF be submitted to this Committee.

In accordance with this requirement, the Director of West Yorkshire Pension Fund submitted **Document "AL"** which reported on the minutes of the meeting of the WYPF Joint Advisory Group held on 31 January 2019.

Members discussed and sought clarification on some of the items in the minutes.

**Resolved –**

**That the minutes of the West Yorkshire Pension Joint Advisory Group held on 31 January 2019 were considered.**

## 58. EXCLUSION OF THE PUBLIC

The Committee was asked to consider if the item relating to the minutes of the meeting of the West Yorkshire Pension Fund Investment Advisory Panel meeting held on 31 January 2019 should be considered in the absence of the public and, if so, to approve the following recommendation:

**Resolved –**

**That the public be excluded from the meeting during the consideration of the items relating to minutes of the West Yorkshire Pension Fund Investment Advisory Panel meeting held on 31 January 2019 because the information to be considered was exempt information within paragraph 3 (Financial or Business Affairs) of Schedule 12A of the Local Government Act 1972. It was also considered that it was in the public interest to exclude public access to this item.**

## 59. MINUTES OF WEST YORKSHIRE PENSION FUND (WYPF) INVESTMENT ADVISORY PANEL HELD ON 31 JANUARY 2019

The Council's Financial Regulations required the minutes of meetings of the WYPF be submitted to this Committee.

In accordance with this requirement, the Director of West Yorkshire Pension Fund submitted **Not for Publication Document "AM"** which reported on the minutes of the meeting of the WYPF Investment Advisory Panel held on 31 January 2019.

Members discussed and sought clarification on some of the items in the minutes.

**Resolved –**

**That the minutes of the West Yorkshire Pension Fund Investment Advisory Panel held on 31 January 2019 were considered.**

## 60. TREASURY MANAGEMENT STRATEGY STATEMENT, MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL INVESTMENT STRATEGY 2019-20

The Director of Finance submitted **Document "AN"** which reported on the Council's Treasury Management Strategy, Minimum Revenue Provision Policy and Annual Investment Strategy for 2019-20.

It was reported that the Treasury Management Strategy for 2019-20 covered two main areas:

Capital Issues –

- The capital expenditure plans and the associated prudential indicators
- The minimum revenue provision (MRP) policy.

Treasury Management Issues –

- The current treasury position
- Treasury indicators which limited the treasury risk and activities of the Council
- Prospects for interest rates
- The borrowing strategy
- Policy on borrowing in advance of need
- Debt rescheduling
- The investment strategy
- Creditworthiness policy; and
- The policy on use of external service providers

Members were informed that the above elements covered the requirements of the Local Government Act 2003, the CIPFA Prudential Code, Ministry for Housing, Communities and Local Government (MHCLG) MRP Guidance, the CIPFA Treasury Management Code and MHCLG Investment Guide.

It was highlighted that Members of the Committee were provided with training in line with the CIPFA Code which required the Section 151 officer to ensure that members with responsibility for treasury management received adequate training in treasury management. The Council's Treasury Management Adviser, Link Asset Services provided training to Members of the Committee earlier today.

Members were informed that the table at 2.1 of the report summarised the capital expenditure plans and how they were financed either by capital or revenue resources. Any shortfall of resources resulted in a funding borrowing need.

It was reported that the capital expenditure plans set out in Section 2 provided details of the service activity of the Council. The treasury management function ensured that the Council's cash was organised in accordance with the relevant professional codes, so that sufficient cash was available to meet this service activity and the Council's expenditure plans. This would involve both the organisation of the cash flow and, where capital plans require, the organisation of appropriate borrowing facilities. This strategy covered the relevant treasury/prudential indicators, the current and projected debt positions and the annual investment strategy.

The overall treasury management portfolio for borrowing and investments as at 31 March 2018 and 31January 2019 was shown in paragraph 3.1.

Members were informed that within the range of prudential indicators there were a number of key indicators to ensure that the Council operated its activities within well-defined limits. One of these was that the Council needed to ensure that its gross debt did not, except in the short term, exceed the total of the CFR (Capital Financing Requirement) in the preceding year plus the estimates of the following two financial years. This allowed some flexibility for limited early borrowing for future years, but ensured that borrowing was not undertaken for revenue or speculative purposes.

It was reported that the Council complied with this prudential indicator in the current year and did not envisage difficulties for the future. This view took into account current commitments, existing plans, and the proposals in the budget report.

Members were informed that the Council was currently maintaining an under-borrowed position. This meant that the capital borrowing need (the Capital Financing Requirement), had not been fully funded with loan debt as cash supporting the Council's reserves, balances and cash flow had been used as a temporary measure. This strategy was prudent as investment returns were low and counterparty risk was still an issue that needed to be considered.

It was reported that the Council's cash balances were expected to reduce since there was a future draw on cash from the Capital Investment Plan. There would be a requirement to borrow in 2019-20. Cash balances and capital spend would be closely monitored and projected forward. As it was felt that cash balances were getting too low or likely to be too low in the future, borrowing would be undertaken in appropriate tranches. In deciding the appropriate tranches of borrowing, caution would be exercised in projecting forward capital spend.

Members were informed that the Director of Finance would monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- If it was felt that there was a significant risk of a sharp fall in long and short term rates, then long term borrowings would be postponed, and potential rescheduling from fixed rate funding into short term borrowing would be considered.
- If it was felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecasted, perhaps arising from an acceleration in the start date and in the rate of increase in central rates in the USA and UK, an increase in world economic activity or a sudden increase in inflation risks, then the portfolio position would be re-appraised. Most likely, fixed rate funding would be drawn whilst interest rates were lower than they were projected to be in the next few years.

It was reported that any decisions made in relation to the above would be reported to the appropriate decision making body at the next available opportunity.

Members were informed that as short-term borrowing rates would be considerably cheaper than longer term fixed interest rates, there may be potential opportunities to generate savings by switching from long-term debt to short-term debt. However, these savings would need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred).

It was reported that Legislative change had been put in place by the government aimed at strengthening the financial system. One of these reforms was to separate the retail banking (ringfenced bank) from the investing banking (unringfenced bank) All the four major banks had to go through this process.

Schools balances would be in the retail or ringfenced part of the bank for Lloyds, Nat West and HSBC but not for Barclays.

This raised the following issues:

- The credit rating for the Barclays unringfenced part of the bank was slightly lower than for the ring fenced bank.
- If the credit rating was to reduce in the future it could be below the Council's credit limit.

Members were informed that further school conversions to Academies on an on going basis was expected and for cash balances held by schools in their bank accounts to steadily reduce as a result. Once converted to academies their bank balances no longer counted towards the Council Treasury limits.

It was reported that given the above changes in status for the schools and the reduction in school balances, it was proposed that the schools continue to have a temporary exemption from the Treasury Policy until the main conversion process had been finished. The Council would inform the schools of the developments in regards to Barclays.

In response to a Member's question as to why revenue was being used to finance capital spend it was reported that £1.2m would be used in this way in 2018-19. This was based on a set of criteria and was a very small element of the revenue budget. Also this avoided generating a borrowing need.

In response to a Member's question in relation to the flexibility to use capital receipts for transformation projects it was reported that the Authority already used its capital receipts to fund capital budgets; if the authority used capital receipts to fund the revenue budget, it would instead borrow more and incur higher interest costs to the capital budget; using capital receipts flexibly to fund revenue also required the criteria to be met that spend was on one-off projects.

There was a short discussion on the principal risks associated with treasury management and the mitigation of those risks as detailed at section 7.1 of the report. It was emphasised that it was crucial that security of an investment was the top priority when considering risk and return around investments.

**Resolved-**

**That the details in the report be noted and Document "AN" be referred to the 19 March 2019 Council meeting for adoption.**

**Action: Director of Finance**

Chair

**Note: These minutes are subject to approval as a correct record at the next meeting of the Governance and Audit Committee.**