South Somerset District Council

Public Document Pack

Informal Consultative meeting of Audit Committee

Thursday 27th May 2021

10.00 am

A virtual consultative meeting via Zoom Meeting Software

The following members are requested to attend this meeting:

Chairman: Martin Carnell
Vice-chairman: Mike Hewitson

Robin Bastable	Malcolm Cavill	Paul Maxwell
Mike Best	Brian Hamilton	Jeny Snell
Dave Bulmer	Tim Kerley	

Any members of the public wishing to address the meeting at Public Question Time need to email democracy@southsomerset.gov.uk by 9.00am Wednesday 26th May 2021.

The meeting will be viewable online by selecting the committee meeting at:
https://www.youtube.com/channel/UCSDst3IHGj9WoGnwJGF_soA

For further information on the items to be discussed, contact
democracy@southsomerset.gov.uk

This Agenda was issued on Wednesday 19 May 2021.

Alex Parmley, *Chief Executive Officer*

This information is also available on our website www.southsomerset.gov.uk and via the mod.gov app

Information for the Public

The purpose of the Audit Committee is to provide independent assurance of the adequacy of the risk management framework and the associated control environment, independent scrutiny of the authority's financial and non-financial performance, to the extent that it affects the authority's exposure to risk and weakens the control environment and to oversee the financial reporting process.

The Audit Committee should review the Code of Corporate Governance seeking assurance where appropriate from the Executive or referring matters to management on the scrutiny function.

The terms of reference of the Audit Committee are:

Internal Audit Activity

1. To approve the Internal Audit Charter and annual Internal Audit Plan;
2. To receive quarterly summaries of Internal Audit reports and seek assurance from management that action has been taken;
3. To receive an annual summary report and opinion, and consider the level of assurance it provides on the council's governance arrangements;
4. To monitor the action plans for Internal Audit reports assessed as "partial" or "no assurance;"
5. To consider specific internal audit reports as requested by the Head of Internal Audit, and monitor the implementation of agreed management actions;
6. To receive an annual report to review the effectiveness of internal audit to ensure compliance with statutory requirements and the level of assurance it provides on the council's governance arrangements;

External Audit Activity

7. To consider and note the annual external Audit Plan and Fees;
8. To consider the reports of external audit including the Annual Audit Letter and seek assurance from management that action has been taken;

Regulatory Framework

9. To consider the effectiveness of SSDC's risk management arrangements, the control environment and associated anti-fraud and corruption arrangements and seek assurance from management that action is being taken;
10. To review the Annual Governance Statement (AGS) and monitor associated action plans;
11. To review the Local Code of Corporate Governance and ensure it reflects best governance practice. This will include regular reviews of part of the Council's Constitution and an overview of risk management;
12. To receive reports from management on the promotion of good corporate governance;

Financial Management and Accounts

13. To review and approve the annual Statement of Accounts, external auditor's opinion and reports to members and monitor management action in response to issues raised;

14. To provide a scrutiny role in Treasury Management matters including regular monitoring of treasury activity and practices. The committee will also review and recommend the Annual Treasury Management Strategy Statement and Investment Strategy, MRP Strategy, and Prudential Indicators to Council;

15. To review and recommend to Council changes to Financial Procedure Rules and Procurement Procedure Rules;

Overall Governance

16. The Audit Committee can request of the Section 151 Officer, the Monitoring Officer, or the Chief Executive (Head of Paid Services) a report (including an independent review) on any matter covered within these Terms of Reference;

17. The Audit Committee will request action through District Executive if any issue remains unresolved;

18. The Audit Committee will report to each full Council a summary of its activities.

Members questions on reports prior to the Meeting

Members of the Committee are requested to contact report authors on points of clarification prior to the Committee meeting.

Audit Committee

Meetings of the Audit Committee are usually held bi-monthly including at least one meeting with the Council's external auditor, although in practice the external auditor attends more frequently. However during the coronavirus pandemic these meetings will be held remotely via Zoom video-conferencing and the starting time may vary.

At the meeting of Full Council on Friday 15th April 2021 it was agreed to extend the delegation of all Executive and Quasi Judicial decisions listed in the Constitution to the Chief Executive and to the relevant Director in the Chief Executive's absence where not already delegated, in consultation with the Leader of the Council (or Deputy) and the relevant Portfolio Holder, Ward Member and Committee Member if practicable to ensure that the Council can continue to operate on-line meetings.

Agendas and minutes of this committee are published on the Council's website at http://modgov.southsomerset.gov.uk/ieDocHome.aspx?bcr=1

Agendas and minutes can also be viewed via the mod.gov app (free) available for iPads and Android devices. Search for 'mod.gov' in the app store for your device, install, and select 'South Somerset' from the list of publishers and then select the committees of interest. A wi-fi signal will be required for a very short time to download an agenda but once downloaded, documents will be viewable offline.

Public participation at meetings (held via Zoom)

Public question time

We recognise that these are challenging times but we still value the public's contribution to our virtual meetings.

If you would like to address the virtual meeting during Public Question Time, please email democracy@southsomerset.gov.uk by 9.00am on Wednesday 26th May 2021. When you have registered, the Chairman will invite you to speak at the appropriate time during the virtual meeting.

The period allowed for participation in Public Question Time shall not exceed 15 minutes except with the consent of the Chairman and members of the Committee. Each individual speaker shall be restricted to a total of three minutes.

This meeting will be streamed online via YouTube at:
https://www.youtube.com/channel/UCSDst3IHGj9WoGnwJGF_soA

Virtual meeting etiquette:

- Consider joining the meeting early to ensure your technology is working correctly.
- Please note that we will mute all public attendees to minimise background noise. If you have registered to speak during the virtual meeting, the Chairman or Administrator will un-mute your microphone at the appropriate time. We also respectfully request that you turn off video cameras until asked to speak.
- Each individual speaker shall be restricted to a total of three minutes.
- When speaking, keep your points clear and concise.
- Please speak clearly – the Councillors are interested in your comments.

Recording and photography at council meetings

Recording of council meetings is permitted, however anyone wishing to do so should let the Chairperson of the meeting know prior to the start of the meeting. The recording should be overt and clearly visible to anyone at the meeting, but non-disruptive. If someone is recording the meeting, the Chairman will make an announcement at the beginning of the meeting. If anyone making public representation does not wish to be recorded they must let the Chairperson know.

The full 'Policy on Audio/Visual Recording and Photography at Council Meetings' can be viewed online at:
http://modgov.southsomerset.gov.uk/documents/s3327/Policy%20on%20the%20recording%20of%20council%20meetings.pdf

Informal Consultative Meeting of Audit Committee

Thursday 27 May 2021

Agenda

Preliminary Items

1. **Apologies for absence**

2. **Declarations of Interest**

   In accordance with the Council's current Code of Conduct (as amended 26 February 2015), which includes all the provisions relating to Disclosable Pecuniary Interests (DPI), personal and prejudicial interests, Members are asked to declare any DPI and also any personal interests (and whether or not such personal interests are also "prejudicial") in relation to any matter on the agenda for this meeting.

3. **Public question time**

4. **Date of next meeting**

   Councillors are requested to note that the next Audit Committee meeting is scheduled to be held at 10.00am on Thursday 29th July 2021.

Items for Discussion

5. **Consultation on Funding Strategy Statement** (Pages 6 - 65)

6. **External Audit Plan for 2020/21 Accounts** (Pages 66 - 91)

7. **Internal Audit Plan 2020/21 Outturn** (Pages 92 - 107)

8. **Internal Audit Annual Opinion Report 2020/21** (Pages 108 - 126)

9. **Annual Treasury Management Activity Report 2020/21** (Pages 127 - 151)

10. **Risk Management Update** (Pages 152 - 156)

11. **Review of the Audit Committee's Terms of Reference** (Pages 157 - 160)

12. **Audit Committee Forward Plan** (Pages 161 - 162)

South Somerset District Council

Consultation on Pension Fund Strategy Statement

Strategic Director:	Nicola Hix, Director Support Services & Strategy
Lead Officer:	Karen Watling, Interim S151 Officer
Contact Details:	Karen.Watling@southsomerset.gov.uk

Purpose of the Report

To seek any comments the Audit Committee may have on Somerset County Council's revised Pension Fund Strategy Statement.

Public Interest

South Somerset District Council is an employer within the Somerset County Council (SCC) Pension Fund.

The Pension Fund has a number of policies contained within the Strategy Statement that it is legally required to maintain and review. There is also a requirement for the administering authority for the Fund (SCC) to consult other relevant stakeholders regarding the policies, including SSDC as an employer within the Fund.

Recommendations

That SSDC notes the new proposed Strategy Statement for the Somerset County Council Pension Fund shown in Appendix A.

Background

The appendix presents the revised Funding Strategy Statement for the Somerset County Council Pension Fund.

Somerset County Council are seeking any comments from employers within the Pension Fund regarding the Strategy Statement.

The Statement has been prepared in accordance with Regulation 58 of the Local Government Pension Scheme Regulations 2013 as amended (the Regulations) and describes Somerset County Council's strategy, in its capacity as administering authority, for the funding of the Somerset County Council Pension Fund.

The Fund's employers and the Fund Actuary, Barnett Waddingham LLP, have been consulted on the contents of this statement.

This statement has also been prepared with regard to the guidance "*Preparing and Maintaining a funding strategy statement in the LGPS" (*2016 edition*)* issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

The Pension Fund Strategy Statement governs how the Fund seeks to ensure it meets its pension payment obligations through time and is a key document regarding the tri-annual valuation undertaken by the Fund's actuary. The new version contains specific separate policies on Contribution reviews and Debt Deferment Agreements / debt spreading agreements.

Report

The revised strategy is shown in Appendix A. Audit Committee is being asked if it has any comments or questions on the revised Strategy Statement being proposed by the administering authority (SCC). This is because the Pension Fund's costs and future liabilities have a large impact on SSDC's finances. It is therefore felt that Audit Committee may, in understanding the Strategy Statement, have a deeper appreciation of the relevant figures in the Council's annual Statement of Accounts and therefore be better able to discharge their annual scrutiny and review of the Accounts.

It should be noted that the interim S151 Officer has no comments to make on the Strategy Statement and that Mr Anton Sweet, Funds & Investments Manager at Somerset County Council, will present the key aspects of the Strategy to the Audit Committee and answer any questions raised.

The revised Statement has been reviewed by the Pensions Committee and they are due to be review it again and adopt it at their next meeting. Any comments from employers such as SSDC need to be made by Friday 28th May 2021.

Financial Implications

There are no direct financial implications arising from agreeing this report.

Council Plan Implications

The proposals in this report contribute to SSDC's vision of being open and transparent and actively communicating, engaging and listening to feedback.

Carbon Emissions and Climate Change Implications

There are no implications arising from agreeing this report.

Equality and Diversity Implications

There are no implications arising from agreeing this report.

Background Papers

*"Preparing and Maintaining a funding strategy statement in the LGPS" (*2016 edition*)* Chartered Institute of Public Finance and Accountancy (CIPFA).

Somerset County Council Pension Fund Funding Strategy Statement

Contents

Introduction

This is the Funding Strategy Statement for the Somerset County Council Pension Fund (the Fund). It has been prepared in accordance with Regulation 58 of the Local Government Pension Scheme Regulations 2013 as amended (the Regulations) and describes Somerset County Council's strategy, in its capacity as administering authority, for the funding of the Somerset County Council Pension Fund.

The Fund's employers and the Fund Actuary, Barnett Waddingham LLP, have been consulted on the contents of this statement.

This statement should be read in conjunction with the Fund's Investment Strategy Statement (ISS) and has been prepared with regard to the guidance (*Preparing and Maintaining a funding strategy statement in the LGPS 2016 edition)* issued by the Chartered Institute of Public Finance and Accountancy (CIPFA).

Purpose of the Funding Strategy Statement

The purpose of this Funding Strategy Statement (FSS) is to:

- Establish a clear and transparent fund-specific strategy that will identify how employers' pension liabilities are best met going forward;
- Support the desirability of maintaining as nearly constant a primary contribution rate as possible, as defined in Regulation 62(6) of the Regulations;
- Ensure that the regulatory requirements to set contributions to meet the future liability to provide Scheme member benefits in a way that ensures the solvency and long-term cost efficiency of the Fund are met; and
- Take a prudent longer-term view of funding those liabilities.

Aims and purpose of the Fund

The aims of the Fund are to:

- Manage employers' liabilities effectively and ensure that sufficient resources are available to meet all liabilities as they fall due;
- Enable primary contribution rates to be kept as nearly constant as possible and (subject to the administering authority not taking undue risks) at reasonable cost to all relevant parties (such as the taxpayers, scheduled, resolution and admitted bodies), while achieving and maintaining Fund solvency and long-term cost efficiency, which should be assessed in light of the risk profile of the Fund and employers, and the risk appetite of the administering authority and employers alike; and
- Seek returns on investment within reasonable risk parameters.

The purpose of the Fund is to:

- Pay pensions, lump sums and other benefits to Scheme members as provided for under the Regulations;
- Meet the costs associated in administering the Fund; and
- Receive and invest contributions, transfer values and investment income.

Funding objectives

Contributions are paid to the Fund by Scheme members and the employing bodies to provide for the benefits which will become payable to Scheme members when they fall due.

The funding objectives are to:

- Ensure that pension benefits can be met as and when they fall due over the lifetime of the Fund;
- Ensure the solvency of the Fund;
- Set levels of employer contribution rates to target a 100% funding level over an appropriate time period and using appropriate actuarial assumptions, while taking into account the different characteristics of participating employers;
- Build up the required assets in such a way that employer contribution rates are kept as stable as possible, with consideration of the long-term cost efficiency objective; and
- Adopt appropriate measures and approaches to reduce the risk, as far as possible, to the Fund, other employers and ultimately the taxpayer from an employer defaulting on its pension obligations.

In developing the funding strategy, the administering authority should also have regard to the likely outcomes of the review carried out under Section 13(4)(c) of the Public Service Pensions Act 2013. Section 13(4)(c) requires an independent review of the actuarial valuations of the LGPS funds; this involves reporting on whether the rate of employer contributions set as part of the actuarial valuations are set at an appropriate level to ensure the solvency of the Fund and the long-term cost efficiency of the Scheme so far as relating to the pension Fund. The review also looks at compliance and consistency of the actuarial valuations.

Key parties

The key parties involved in the funding process and their responsibilities are set out below.

<u>The administering authority</u>

The administering authority for the Fund is Somerset County Council. The main responsibilities of the administering authority are to:

- Operate the Fund in accordance with the LGPS Regulations;
- Collect employee and employer contributions, investment income and other amounts due to the Fund as stipulated in the Regulations;
- Invest the Fund's assets in accordance with the Fund's Investment Strategy Statement;
- Pay the benefits due to Scheme members as stipulated in the Regulations;
- Ensure that cash is available to meet liabilities as and when they fall due;
- Take measures as set out in the Regulations to safeguard the Fund against the consequences of employer default;
- Manage the actuarial valuation process in conjunction with the Fund Actuary;
- Prepare and maintain this FSS and also the ISS after consultation with other interested parties;
- Monitor all aspects of the Fund's performance;
- Effectively manage any potential conflicts of interest arising from its dual role as both Fund administrator and Scheme employer; and
- Enable the Local Pension Board to review the valuation process as they see fit.

Scheme employers

In addition to the administering authority, a number of other Scheme employers participate in the Fund.

The responsibilities of each employer that participates in the Fund, including the administering authority, are to:

- Collect employee contributions and pay these together with their own employer contributions, as certified by the Fund Actuary, to the administering authority within the statutory timescales;
- Notify the administering authority of any new Scheme members and any other membership changes promptly;
- Develop a policy on certain discretions and exercise those discretions as permitted under the Regulations;
- Meet the costs of any augmentations or other additional costs in accordance with agreed policies and procedures; and
- Pay any exit payments due on ceasing participation in the Fund.

Scheme members

Active Scheme members are required to make contributions into the Fund as set by the Ministry of Housing, Communities and Local Government (MHCLG).

Fund Actuary

The Fund Actuary for the Fund is Barnett Waddingham LLP. The main responsibilities of the Fund Actuary are to:

- Prepare valuations including the setting of employers' contribution rates at a level to ensure Fund solvency and long-term cost efficiency after agreeing assumptions with the administering authority and having regard to the FSS and the Regulations;
- Prepare advice and calculations in connection with bulk transfers and the funding aspects of individual benefit-related matters such as pension strain costs, ill-health retirement costs, compensatory added years costs, etc;
- Provide advice and valuations on the exiting of employers from the Fund;
- Provide advice and valuations relating to new employers, including recommending the level of bonds or other forms of security required to protect the Fund against the financial effect of employer default;
- Assist the administering authority in assessing whether employer contributions need to be revised between valuations as permitted or required by the Regulations;
- Ensure that the administering authority is aware of any professional guidance or other professional requirements which may be of relevance to their role in advising the Fund; and
- Advise on other actuarial matters affecting the financial position of the Fund.

Funding strategy

The factors affecting the Fund's finances are constantly changing, so it is necessary for its financial position and the contributions payable to be reviewed from time to time by means of an actuarial valuation to check that the funding objectives are being met.

The most recent actuarial valuation of the Fund was carried out as at 31 March 2019. The results of the 2019 valuation are set out in the table below:

2019 valuation results	
Surplus (Deficit)	(£362m)
Funding level	86%

On a whole Fund level, the primary rate required to cover the employer cost of future benefit accrual was 17.8% of payroll p.a.

The individual employer contribution rates are set out in the Rates and Adjustments Certificate which forms part of the Fund's 2019 valuation report.

The actuarial valuation involves a projection of future cashflows to and from the Fund. The main purpose of the valuation is to determine the level of employers' contributions that should be paid to ensure that the existing assets and future contributions will be sufficient to meet all future benefit payments from the Fund. A summary of the methods and assumptions adopted is set out in the sections below.

Funding method

The key objective in determining employers' contribution rates is to establish a funding target and then set levels of employer contribution rates to meet that target over an agreed period.

The funding target is to have sufficient assets in the Fund to meet the accrued liabilities for each employer in the Fund.

For all employers, the method adopted is to consider separately the benefits accrued before the valuation date (past service) and benefits expected to be accrued after the valuation date (future service). These are evaluated as follows:

- The past service funding level of the Fund. This is the ratio of accumulated assets to liabilities in respect of past service. It makes allowance for future increases to members' pay and pensions. A funding level in excess of 100% indicates a surplus of assets over liabilities; while a funding level of less than 100% indicates a deficit; and
- The future service funding rate (also referred to as the primary rate as defined in Regulation 62(5) of the Regulations) is the level of contributions required from the individual employers which, in combination with employee contributions is expected to cover the cost of benefits accruing in future.

The adjustment required to the primary rate to calculate an employer's total contribution rate is referred to as the secondary rate, as defined in Regulation 62(7). Further details of how the secondary rate is calculated for employers is given below.

The approach to the primary rate will depend on specific employer circumstances and in particular may depend on whether an employer is an "open" employer – one which allows new recruits access to the Fund, or a "closed" employer – one which no longer permits new staff access to the Fund. The expected period of participation by an employer in the Fund may also affect the total contribution rate.

For open employers, the actuarial funding method that is adopted is known as the Projected Unit Method. The key feature of this method is that, in assessing the future service cost, the primary rate represents the cost of one year's benefit accrual only.

For closed employers, the actuarial funding method adopted is known as the Attained Age Method. The key difference between this method and the Projected Unit Method is that the Attained Age Method assesses the average cost of the benefits that will accrue over a specific period, such as the length of a contract or the remaining expected working lifetime of active members.

The approach by employer may vary to reflect an employer's specific circumstance. However, in general the closed employers in the Fund are admission bodies who have joined the Fund as part of an outsourcing contract and therefore the Attained Age Method is used in setting their contributions. All other employers (for example councils, higher education bodies and academies) are generally open employers and therefore the Projected Unit Method is used. The administering authority holds details of the open or closed status of each employer.

Valuation assumptions and funding model

In completing the actuarial valuation it is necessary to formulate assumptions about the factors affecting the Fund's future finances such as price inflation, pay increases, investment returns, rates of mortality, early retirement and staff turnover etc.

The assumptions adopted at the valuation can therefore be considered as:

- The demographic (or statistical) assumptions which are essentially estimates of the likelihood or timing of benefits and contributions being paid, and
- The financial assumptions which will determine the estimates of the amount of benefits and contributions payable and their current (or present) value.

Future price inflation

The base assumption in any valuation is the future level of price inflation over a period commensurate with the duration of the liabilities, as measured by the Retail Price Index (RPI). This is derived using the 20 year point on the Bank of England implied Retail Price Index (RPI) inflation curve, with consideration of the market conditions over the six months straddling the valuation date. The 20 year point on the curve is taken as 20 years is consistent with the average duration of an LGPS Fund. The RPI assumption adopted as at 31 March 2019 was 3.6% p.a.

This assumption was reviewed following the Chancellor's announcement on the reform of RPI in November 2020. From 31 December 2020 RPI inflation is assumed to be 0.4% p.a. lower than the 20 year point on the inflation curve. This adjustment accounts for both the shape of the curve in comparison to the Fund's liability profile and the view that investors are willing to accept a lower return on investments to ensure inflation linked returns.

Future pension increases

Pension increases are linked to changes in the level of the Consumer Price Index (CPI). Inflation as measured by the CPI has historically been less than RPI due mainly to different calculation methods.

At the 31 March 2019 actuarial valuation a deduction of 1.0% p.a. was therefore made to the RPI assumption to derive the CPI assumption. The CPI assumption adopted as at 31 March 2019 was 2.6% p.a.

This assumption was also reviewed in light of the Chancellor's announcement on the reform of RPI mentioned above. From 31 December 2020 CPI inflation is assumed to be 0.4% p.a. lower than the RPI assumption (i.e. 0.8% p.a. below the 20 year point on the Bank of England implied RPI inflation curve). This reflects the anticipated reform of RPI inflation from 2030 following the UK Statistics Authority's proposal to change how RPI is calculated to bring it in line with the Consumer Prices Index including Housing costs (CPIH). This assumption will be reviewed at future valuations and the difference between RPI and CPI is expected to move towards 0.0% p.a. as we get closer to 2030.

Future pay increases

As some of the benefits are linked to pay levels at retirement, it is necessary to make an assumption as to future levels of pay increases. Historically, there has been a close link between price inflation and pay increases with pay increases exceeding price inflation in the longer term. The long-term pay increase assumption adopted as at 31 March 2019 was CPI plus 1.0% p.a. which includes allowance for promotional increases.

Future investment returns/discount rate

To determine the value of accrued liabilities and derive future contribution requirements it is necessary to discount future payments to and from the Fund to present day values.

The discount rate that is adopted will depend on the funding target adopted for each Scheme employer.

For open employers, the discount rate that is applied to all projected liabilities reflects a prudent estimate of the rate of investment return that is expected to be earned from the underlying investment strategy by considering average market yields in the six months straddling the valuation date. The discount rate so determined may be referred to as the "ongoing" discount rate. The discount rate adopted for the 31 March 2019 valuation was 4.9% p.a.

For closed employers, an adjustment may be made to the discount rate in relation to the remaining liabilities, once all active members are assumed to have retired if at that time (the projected "termination date"), the employer becomes an exiting employer under Regulation 64.

The Fund Actuary will incorporate such an adjustment after consultation with the administering authority.

The adjustment to the discount rate for closed employers may be set to a higher funding target at the projected termination date, so that there are sufficient assets to fund the remaining liabilities on a "minimum risk" rather than on an ongoing basis if the Fund does not believe that there is another Scheme employer to take on the responsibility of the liabilities after the employer has exited the Fund. The aim is to minimise the risk of deficits arising after the termination date.

It may be appropriate for an alternative discount rate approach to be taken to reflect an individual employer's situation. This may be, for example, to reflect an employer targeting a cessation event or to reflect the administering authority's views on the level of risk that an employer poses to the Fund. The Fund Actuary will incorporate any such adjustments after consultation with the administering authority.
A summary of the financial assumptions adopted for the 2019 valuation is set out in the table below:

Financial assumptions as at 31 March 2019	
RPI inflation	3.6% p.a.
CPI inflation	2.6% p.a.
Pension/deferred pension increases and CARE revaluation	In line with CPI inflation
Pay increases	CPI inflation + 1.0% p.a.
Discount rate	4.9% p.a.

<u>Asset valuation</u>

For the purpose of the valuation, the asset value used is the market value of the accumulated fund at the valuation date, adjusted to reflect average market conditions during the six months straddling the valuation date. This is referred to as the smoothed asset value and is calculated as a consistent approach to the valuation of the liabilities.

The Fund's assets are notionally allocated to employers at an individual level by allowing for actual Fund returns achieved on the assets and cashflows paid into and out of the Fund in respect of each employer (e.g. contributions received and benefits paid).

<u>Demographic assumptions</u>

The demographic assumptions incorporated into the valuation are based on Fund-specific experience and national statistics, adjusted as appropriate to reflect the individual circumstances of the Fund and/or individual employers.

Further details of the assumptions adopted are included in the Fund's 2019 valuation report.

McCloud/Sargeant judgements

The McCloud/Sargeant judgements were in relation to two employment tribunal cases which were brought against the government in relation to possible age and gender discrimination in the implementation of transitional protection following the introduction of the reformed 2015 public service pension schemes from 1 April 2015. These judgements were not directly in relation to the LGPS, however, do have implications for the LGPS.

In December 2018, the Court of Appeal ruled that the transitional protection offered to some members as part of the reforms amounted to unlawful discrimination. On 27 June 2019 the Supreme Court denied the government's request for an appeal in the case, and on 15 July 2019 the Government released a statement to confirm that it expects to have to amend all public service schemes, including the LGPS. On 16 July 2020, the Government published a consultation on the proposed remedy to be applied to LGPS benefits and at the same time announced the unpausing of the 2016 cost cap process which will take into account the remedy for the McCloud and Sargeant judgement. The consultation closed on 8 October 2020 and the final remedy will only be known after the consultation responses have been reviewed and a final set of remedial Regulations are published.

Further details of this can be found below in the Regulatory risks section.

As part of the Fund's 2019 valuation, in order to mitigate the risk of member benefits being uplifted and becoming more expensive, the potential impact of McCloud was covered by the prudence allowance in the discount rate assumption. As the remedy is still to be agreed the cost cannot be calculated with certainty, however, the Fund Actuary expects it is likely to be less than 0.05% of the discount rate assumption.

Guaranteed Minimum Pension (GMP) indexation and equalisation

As part of the restructuring of the state pension provision, the government needs to consider how public service pension payments should be increased in future for members who accrued a Guaranteed Minimum Pension (GMP) from their public service pension scheme and expect to reach State Pension Age (SPA) post-December 2018. In addition, a resulting potential inequality in the payment of public service pensions between men and women needs to be addressed. Information on the current method of indexation and equalisation of public service pension schemes can be found here.

On 22 January 2018, the government published the outcome to its *Indexation and equalisation of GMP in public service pension schemes* consultation, concluding that the requirement for public service pension schemes to fully price protect the GMP element of individuals' public service pension would be extended to those individuals reaching SPA before 6 April 2021. HMT published a Ministerial Direction on 4 December 2018 to implement this outcome, with effect from 6 April 2016. Details of this outcome and the Ministerial Direction can be found here.

The 2019 valuation assumption for GMP is that the Fund will pay limited increases for members that have reached SPA by 6 April 2016, with the government providing the remainder of the inflationary increase. For members that reach SPA after this date, it is assumed that the Fund will be required to pay the entire inflationary increase.

Contribution reviews between actuarial valuations

It is anticipated for most Scheme employers that the contribution rates certified at the formal actuarial valuation will remain payable for the period of the rates and adjustments certificate. However, there may be circumstances where a review of the contribution rates payable by an employer (or a group of employers) under Regulation 64A is deemed appropriate by the administering authority.

A contribution review may be requested by an employer or be required by the administering authority. The review may only take place if one of the following conditions are met:

(i) it appears likely to the administering authority that the amount of the liabilities arising or likely to arise has changed significantly since the last valuation;

(ii) it appears likely to the administering authority that there has been a significant change in the ability of the Scheme employer or employers to meet the obligations of employers in the Scheme; or

(iii) a Scheme employer or employers have requested a review of Scheme employer contributions and have undertaken to meet the costs of that review. A request under this condition can only be made if there has been a significant change in the liabilities arising or likely to arise and/or there has been a significant change in the ability of the Scheme employer to meet its obligations to the Fund.

Guidance on the administering authority's approach considering the appropriateness of a review and the process in which a review will be conducted is set out the Fund's separate Contribution review policy which, is attached as appendix A. This includes details of the process that should be followed where an employer would like to request a review.

Once a review of contribution rates has been agreed, unless the impact of amending the contribution rates is deemed immaterial by the Fund Actuary, then the results of the review will be applied with effect from the agreed review date, regardless of the direction of change in the contribution rates.

Note that where a Scheme employer seems likely to exit the Fund before the next actuarial valuation then the administering authority can exercise its powers under Regulation 64(4) to carry out a review of contributions with a view to providing that assets attributable to the Scheme employer are equivalent to the exit payment that will be due from the Scheme employer. These cases do not fall under the separate contribution review policy.

With the exception of any cases falling under Regulation 64(4), the administering authority will not accept a request for a review of contributions where the effective date is within 12 months of the next rates and adjustments certificate.

Deficit recovery/surplus amortisation periods

Whilst one of the funding objectives is to build up sufficient assets to meet the cost of benefits as they accrue, it is recognised that at any particular point in time, the value of the accumulated assets will be different to the value of accrued liabilities, depending on how the actual experience of the Fund differs to the actuarial assumptions. This theory applies down to an individual employer level; each employer in the Fund has their own share of deficit or surplus attributable to their section of the Fund.

Where the valuation for an employer discloses a surplus or deficit then the levels of required employer contributions will include an adjustment to either amortise the surplus or fund the deficit over a period of years.

The recovery periods adopted for the employers in the Fund for the 2019 valuation varied from 3 years to 19 years. This represents a reduction of five years from the maximum 24 year recovery period set at the 2016 valuation. The ultimate aim is to reach 100% funding, and a reduction of in the recovery period since the 2016 valuation demonstrates that the Fund is progressing towards that goal. Please note that recovery periods varied between individual employers. The adjustment may be set either as a percentage of payroll or as a fixed monetary amount. The period that is adopted for any particular employer will depend on:

- The significance of the surplus or deficit relative to that employer's liabilities;
- The covenant of the individual employer (including any security in place) and any limited period of participation in the Fund;
- The remaining contract length of an employer in the Fund (if applicable); and
- The implications in terms of stability of future levels of employers' contribution.

Pooling of individual employers

The policy of the Fund is that each individual employer should be responsible for the costs of providing pensions for its own employees who participate in the Fund. Accordingly, contribution rates are set for individual employers to reflect their own particular circumstances.

However, certain groups of individual employers are pooled for the purposes of determining contribution rates to recognise common characteristics or where the number of Scheme members is small.

The funding pools adopted for the Fund at the 2019 valuation are summarised in the table below:

Pool	Type of pooling	Notes
Academies	Past and future service pooling	All academies in the pool pay the same total contribution rate and have the same funding level
Small Scheduled bodies	Past and future service pooling	All town and parish councils in the pool pay the same primary rate but pay a secondary rate bespoke to their position
NSL Ltd	Past and future service pooling	All employers in the pool pay the same total contribution rate and have the same funding level
BAM FM	Past and future service pooling	All employers in the pool pay the same total contribution rate and have the same funding level

The main purpose of pooling is to produce more stable employer contribution levels, although recognising that ultimately there will be some level of cross-subsidy of pension cost amongst pooled employers.

<u>Forming/disbanding a funding pool</u>

Where the Fund identifies a group of employers with similar characteristics and potential merits for pooling, it is possible to form a pool for these employers. Advice will be sought from the Fund Actuary to consider the appropriateness and practicalities of forming the funding pool.

Conversely, the Fund may consider it no longer appropriate to pool a group of employers. This could be due to divergence of previously similar characteristics or an employer becoming a dominant party in the pool (such that the results of the pool are largely driven by that dominant employer). Where this scenario arises, advice will be sought from the Fund Actuary.

Funding pools should be monitored on a regular basis, at least at each actuarial valuation, in order to ensure the pooling arrangement remains appropriate.

Risk-sharing

There are employers that participate in the Fund with a risk-sharing arrangement in place with another employer in the Fund.

At the 2019 valuation, risk-sharing arrangements were allowed for by allocating any deficit/liabilities covered by the risk-sharing arrangement to the relevant responsible employer.

New employers joining the Fund

When a new employer joins the Fund, the Fund Actuary is required to set the contribution rates payable by the new employer and allocate a share of Fund assets to the new employer as appropriate. The most common types of new employers joining the Fund are admission bodies and new academies. These are considered in more detail below.

Admission bodies

New admission bodies in the Fund are commonly a result of a transfer of staff from an existing employer in the Fund to another body (for example as part of a transfer of services from a council or academy to an external provider under Schedule 2 Part 3 of the Regulations). Typically these transfers will be for a limited period (the contract length), over which the new admission body employer is required to pay contributions into the Fund in respect of the transferred members.

<u>Funding at start of contract</u>

Generally, when a new admission body joins the Fund, they will become responsible for all the pensions risk associated with the benefits accrued by transferring members and the benefits to be accrued over the contract length. This is known as a full risk transfer. In these cases, it may be appropriate that the new admission body is allocated a share of Fund assets equal to the value of the benefits transferred, i.e. the new admission body starts off on a fully funded basis. This is calculated on the relevant funding basis and the opening position may be different when calculated on an alternative basis (e.g. on an accounting basis).

However, there may be special arrangements made as part of the contract such that a full risk transfer approach is not adopted. In these cases, the initial assets allocated to the new admission body will reflect the level of risk transferred and may therefore not be on a fully funded basis or may not reflect the full value of the benefits attributable to the transferring members.

Contribution rate

The contribution rate may be set on an open or a closed basis. Where the funding at the start of the contract is on a fully funded basis then the contribution rate will represent the primary rate only; where there is a deficit allocated to the new admission body then the contribution rate will also incorporate a secondary rate with the aim of recovering the deficit over an appropriate recovery period.

Depending on the details of the arrangement, for example if any risk sharing arrangements are in place, then additional adjustments may be made to determine the contribution rate payable by the new admission body. The approach in these cases will be bespoke to the individual arrangement.

Security

To mitigate the risk to the Fund that a new admission body will not be able to meet its obligations to the Fund in the future, the new admission body may be required to put in place a bond in accordance with Schedule 2 Part 3 of the Regulations, if required by the letting authority and administering authority.

If, for any reason, it is not desirable for a new admission body to enter into a bond, the new admission body may provide an alternative form of security which is satisfactory to the administering authority.

Risk-sharing

Although a full risk transfer (as set out above) is most common, subject to agreement with the administering authority where required, new admission bodies and the relevant letting authority may make a commercial agreement to deal with the pensions risk differently. For example, it may be agreed that all or part of the pensions risk remains with the letting authority.

Although pensions risk may be shared, it is common for the new admission body to remain responsible for pensions costs that arise from:

- above average pay increases, including the effect on service accrued prior to contract commencement; and
- redundancy and early retirement decisions.

The administering authority may consider risk-sharing arrangements as long as the approach is clearly documented in the admission agreement, the transfer agreement or any other side agreement. The arrangement also should not lead to any undue risk to the other employers in the Fund.

Legal and actuarial advice in relation to risk-sharing arrangements should be sought where required.

New academies

When a school converts to academy status, the new academy (or the sponsoring multi-academy trust) becomes a Scheme employer in its own right.

<u>Funding at start</u>

On conversion to academy status, the new academy will become part of the Academies funding pool and will be allocated assets based on the funding level of the pool at the conversion date.

<u>Contribution rate</u>

The contribution rate payable when a new academy joins the Fund will be in line with the contribution rate certified for the Academies funding pool at the 2019 valuation.

Where an academy joins an existing multi-academy trust in the Fund, additional contributions will be certified for the multi-academy trust in respect of the academy.

Cessation valuations

When a Scheme employer exits the Fund and becomes an exiting employer, as required under the Regulations the Fund Actuary will be asked to carry out an actuarial valuation in order to determine the liabilities in respect of the benefits held by the exiting employer's current and former employees. The Fund Actuary is also required to determine the exit payment due from the exiting employer to the Fund or the exit credit payable from the Fund to the exiting employer.

In assessing the value of the liabilities attributable to the exiting employer, the Fund Actuary may adopt differing approaches depending on the employer and the specific details surrounding the employer's cessation scenario.

Exit payment policy

Where a cessation valuation reveals a deficit and an exit payment is due, the expectation is that the employer settles this debt immediately through a single cash payment. However, should it not be possible for the employer to settle this amount, providing the employer puts forward sufficient supporting evidence to the administering authority, the administering authority may agree a deferred debt agreement (DDA) with the employer under Regulation 64(7A) or a debt spreading agreement (DSA) under Regulation 64B.

Under a DDA, the exiting employer becomes a deferred employer in the Fund (i.e. they remain as a Scheme employer but with no active members) and remains responsible for paying the secondary rate of contributions to fund their deficit. The secondary rate of contributions will be reviewed at each actuarial valuation until the termination of the agreement.

Under a DSA, the cessation debt is crystallised and spread over a period deemed reasonable by the administering authority having regard to the views of the Fund Actuary.

Whilst a DSA involves crystallising the cessation debt and the employer's only obligation is to settle this set amount, in a DDA the employer remains in the Fund as a Scheme employer and is exposed to the same risks (unless agreed otherwise with the administering authority) as active employers in the Fund (e.g. investment, interest rate, inflation, longevity and regulatory risks) meaning that the deficit will change over time.

Guidance on the administering authority's policy for entering into, monitoring and terminating a DDA or DSA is set out in the Fund's separate DSA and DDA policies document attached as Appendix B. This includes details of when a DDA or a DSA may be permitted and the information required from the employer when putting forward a request for a DDA or DSA.

Exit credit policy

Any surplus in the Fund in respect of the exiting employer may be paid from the Fund to the employer as an exit credit, subject to the agreement between the relevant parties and any legal documentation. Having regard to any relevant considerations, the administering authority will take the following approach to the payment of exit credits:

- Any employer who cannot demonstrate that they have been exposed to underfunding risk during their participation in the Fund will not be entitled to an exit credit payment. This will include the majority of "pass-through" arrangements. This is on the basis that these employers would not have not been asked to pay an exit payment had a deficit existed at the time of exit.
- The administering authority does not need to enquire into the precise risk sharing arrangement adopted by an employer but it must be satisfied that the risk sharing arrangement has been in place before it will pay out an exit credit. The level of risk that an employer has borne will be taken into account when determining the amount of any exit credit. It is the responsibility of the exiting employer to set out why the arrangements make payment of an exit credit appropriate.
- Any exit credit payable will be subject to a maximum of the actual employer contributions paid into the Fund.
- As detailed above, the Fund Actuary may adopt differing approaches depending on the employer the specific details surrounding the employer's cessation scenario. The default approach to calculating the cessation position will be on a minimum-risk basis unless it can be shown that there is another employer in the Fund who will take on financial responsibility for the liabilities in the future. If the administering authority is satisfied that there is another employer willing to take on responsibility for the liabilities (or that there is some other form of guarantee in place) then the cessation position may be calculated on the ongoing funding basis.
- The administering authority will pay out any exit credits within six months of the cessation date where possible. A longer time may be agreed between the administering authority and the exiting employer where necessary. For example if the employer does not provide all the relevant information to the administering authority within one month of the cessation date the administering authority will not be able to guarantee payment within six months of the cessation date.
- Under the Regulations, the administering authority has the discretion to take into account any other relevant factors in the calculation of any exit credit payable and they will seek legal advice where appropriate.

Bulk transfers

Bulk transfers of staff into or out of the Fund can take place from other LGPS Funds or non-LGPS Funds. In either case, the Fund Actuary for both Funds will be required to negotiate the terms for the bulk transfer – specifically the terms by which the value of assets to be paid from one Fund to the other is calculated.

The agreement will be specific to the situation surrounding each bulk transfer but in general the Fund will look to receive the bulk transfer on no less than a fully funded transfer (i.e. the assets paid from the ceding Fund are sufficient to cover the value of the liabilities on the agreed basis).

A bulk transfer may be required by an issued Direction Order. This is generally in relation to an employer merger, where all the assets and liabilities attributable to the transferring employer in its original Fund are transferred to the receiving Fund.

Links with the Investment Strategy Statement (ISS)

The main link between the Funding Strategy Statement (FSS) and the ISS relates to the discount rate that underlies the funding strategy as set out in the FSS, and the expected rate of investment return which is expected to be achieved by the long-term investment strategy as set out in the ISS.

As explained above, the ongoing discount rate that is adopted in the actuarial valuation is derived by considering the expected return from the long-term investment strategy. This ensures consistency between the funding strategy and investment strategy.

Risks and counter measures

Whilst the funding strategy attempts to satisfy the funding objectives of ensuring sufficient assets to meet pension liabilities and stable levels of employer contributions, it is recognised that there are risks that may impact on the funding strategy and hence the ability of the strategy to meet the funding objectives.
The major risks to the funding strategy are financial, although there are other external factors including demographic risks, regulatory risks and governance risks.

Financial risks

The main financial risk is that the actual investment strategy fails to produce the expected rate of investment return (in real terms) that underlies the funding strategy. This could be due to a number of factors, including market returns being less than expected and/or the fund managers who are employed to implement the chosen investment strategy failing to achieve their performance targets.

The valuation results are most sensitive to the real discount rate (i.e. the difference between the discount rate assumption and the price inflation assumption). Broadly speaking an increase/decrease of 0.5% p.a. in the real discount rate will decrease/increase the valuation of the liabilities by 10%, and decrease/increase the required employer contribution by around 2.5% of payroll p.a.

However, the Pensions Committee regularly monitors the investment returns achieved by the fund managers and receives advice from the independent advisers and officers on investment strategy.

The Committee may also seek advice from the Fund Actuary on valuation related matters.

In addition, the Fund Actuary provides funding updates between valuations to check whether the funding strategy continues to meet the funding objectives.

Demographic risks

Allowance is made in the funding strategy via the actuarial assumptions for a continuing improvement in life expectancy. However, the main demographic risk to the funding strategy is that it might underestimate the continuing improvement in longevity. For example, an increase of one year to life expectancy of all members in the Fund will reduce the funding level by approximately 1%.

The actual mortality of pensioners in the Fund is monitored by the Fund Actuary at each actuarial valuation and assumptions are kept under review. For the 2019 funding valuation, the Fund commissioned a bespoke longevity analysis by Barnett Waddingham's specialist longevity team in order to assess the mortality experience of the Fund and help set an appropriate mortality assumption for funding purposes.

The liabilities of the Fund can also increase by more than has been planned as a result of the additional financial costs of early retirements and ill-health retirements. However, the administering authority monitors the incidence of early retirements; and procedures are in place that require individual employers to pay additional amounts into the Fund to meet any additional costs arising from early retirements.

Maturity risk

The maturity of a Fund (or of an employer in the Fund) is an assessment of how close on average the members are to retirement (or already retired). The more mature the Fund or employer, the greater proportion of its membership that is near or in retirement. For a mature Fund or employer, the time available to generate investment returns is shorter and therefore the level of maturity needs to be considered as part of setting funding and investment strategies.

The cashflow profile of the Fund needs to be considered alongside the level of maturity: as a Fund matures, the ratio of active to pensioner members falls, meaning the ratio of contributions being paid into the Fund to the benefits being paid out of the Fund also falls. This therefore increases the risk of the Fund having to sell assets in order to meets its benefit payments.

The government has published a consultation (*Local government pension scheme: changes to the local valuation cycle and management of employer risk*) which may affect the Fund's exposure to maturity risk. More information on this can be found in the Regulatory risks section below.

Regulatory risks

The benefits provided by the Scheme and employee contribution levels are set out in Regulations determined by central government. The tax status of the invested assets is also determined by the government.

The funding strategy is therefore exposed to the risks of changes in the Regulations governing the Scheme and changes to the tax regime which may affect the cost to individual employers participating in the Scheme.

However, the administering authority participates in any consultation process of any proposed changes in Regulations and seeks advice from the Fund Actuary on the financial implications of any proposed changes.

There are a number of general risks to the Fund and the LGPS, including:

- If the LGPS was to be discontinued in its current form it is not known what would happen to members' benefits.
- The potential effects of GMP equalisation between males and females, if implemented, are not yet known.
- More generally, as a statutory scheme the benefits provided by the LGPS or the structure of the scheme could be changed by the government.
- The State Pension Age is due to be reviewed by the government in the next few years.

At the time of preparing this FSS, specific regulatory risks of particular interest to the LGPS are in relation to the McCloud/Sargeant judgements, the cost cap mechanism and the timing of future funding valuations consultation. These are discussed in the sections below.

McCloud/Sargeant judgements and cost cap

The 2016 national Scheme valuation was used to determine the results of HM Treasury's (HMT) employer cost cap mechanism for the first time. The HMT cost cap mechanism was brought in after Lord Hutton's review of public service pensions with the aim of providing protection to taxpayers and employers against unexpected changes (expected to be increases) in pension costs. The cost control mechanism only considers "member costs". These are the costs relating to changes in assumptions made to carry out valuations relating to the profile of the Scheme members; e.g. costs relating to how long members are expected to live for and draw their pension. Therefore, assumptions such as future expected levels of investment returns and levels of inflation are not included in the calculation, so have no impact on the cost management outcome.

The 2016 HMT cost cap valuation revealed a fall in these costs and therefore a requirement to enhance Scheme benefits from 1 April 2019. However, as a funded Scheme, the LGPS also had a cost cap mechanism controlled by the Scheme Advisory Board (SAB) in place and HMT allowed SAB to put together a package of proposed benefit changes in order for the LGPS to no longer breach the HMT cost cap. These benefit changes were due to be consulted on with all stakeholders and implemented from 1 April 2019.

However, on 20 December 2018 there was a judgement made by the Court of Appeal which resulted in the government announcing their decision to pause the cost cap process across all public service schemes. This was in relation to two employment tribunal cases which were brought against the government in relation to possible discrimination in the implementation of transitional protection following the introduction of the reformed 2015 public service pension schemes from 1 April 2015. Transitional protection enabled some members to remain in their pre-2015 schemes after 1 April 2015 until retirement or the end of a pre-determined tapered protection period. The claimants challenged the transitional protection arrangements on the grounds of direct age discrimination, equal pay and indirect gender and race discrimination.

The first case (McCloud) relating to the Judicial Pension Scheme was ruled in favour of the claimants, while the second case (Sargeant) in relation to the Fire scheme was ruled against the claimants. Both rulings were appealed and as the two cases were closely linked, the Court of Appeal decided to combine the two cases. In December 2018, the Court of Appeal ruled that the transitional protection offered to some members as part of the reforms amounts to unlawful discrimination. On 27 June 2019 the Supreme Court denied the government's request for an appeal in the case, and on 15 July 2019 the Government released a statement to confirm that it expects to have to amend all public service schemes, including the LGPS. On 16 July 2020, the Government published a consultation on the proposed remedy to be applied to LGPS benefits and at the same time announced the unpausing of the 2016 cost cap process which will take into account the remedy for the McCloud and Sargeant judgement. The consultation closed on 8 October 2020 and the final remedy will only be known after the consultation responses have been reviewed and a final set of remedial Regulations are published.

<u>Consultation: Local government pension scheme: changes to the local valuation cycle and management of employer risk</u>

On 8 May 2019, the government published a consultation seeking views on policy proposals to amend the rules of the LGPS in England and Wales. The consultation covered:

- amendments to the local fund valuations from the current three year (triennial) to a four year (quadrennial) cycle;
- a number of measures aimed at mitigating the risks of moving from a triennial to a quadrennial cycle;
- proposals for flexibility on exit payments;
- proposals for further policy changes to exit credits; and
- proposals for changes to the employers required to offer LGPS membership.

The consultation is currently ongoing: the consultation was closed to responses on 31 July 2019 and an outcome is now awaited. So far, two partial responses to the consultation have been issued:

- On 27 February 2020, a partial response was issued relating to policy changes to exit credits
- On 26 August 2020, a partial response was issued relating to review of employer contributions and flexibility on exit payments

This FSS has been updated in light of these responses and will be revisited again once the outcomes are known for the remaining items.
Detail of the outstanding policy proposals are outlined below:

Timing of future actuarial valuations

LGPS valuations currently take place on a triennial basis which results in employer contributions being reviewed every three years. In September 2018 it was announced by the Chief Secretary to HMT, Elizabeth Truss, that the national Scheme valuation would take place on a quadrennial basis (i.e. every four years) along with the other public sector pension schemes. This results of the national Scheme valuation are used to test the cost control cap mechanism and HMT believed that all public sector scheme should have the cost cap test happen at the same time with the next quadrennial valuation in 2020 and then 2024.

Changes to employers required to offer LGPS membership

At the time of drafting this FSS, under the current Regulations further education corporations, sixth form college corporations and higher education corporations in England and Wales are required to offer membership of the LGPS to their non-teaching staff.

With consideration of the nature of the LGPS and the changes in nature of the further education and higher education sectors, the government has proposed to remove the requirement for further education corporations, sixth form college corporations and higher education corporations in England to offer new employees access to the LGPS. Given the significance of these types of employers in the Fund, this could impact on the level of maturity of the Fund and the cashflow profile. For example, increased risk of contribution income being insufficient to meet benefit outgo, if not in the short term then in the long term as the payroll in respect of these types of employers decreases with fewer and fewer active members participating in the Fund.

This also brings an increased risk to the Fund in relation to these employers becoming exiting employers in the Fund. Should they decide not to admit new members to the Fund, the active membership attributable to the employers will gradually reduce to zero, triggering an exit under the Regulations and a potential significant exit payment. This has the associated risk of the employer not being able to meet the exit payment and thus the exit payment falling to the other employers in the Fund.

Employer risks

Many different employers participate in the Fund. Accordingly, it is recognised that a number of employer-specific events could impact on the funding strategy including:

- Structural changes in an individual employer’s membership;
- An individual employer deciding to close the Scheme to new employees; and
- An employer ceasing to exist without having fully funded their pension liabilities.

However, the administering authority monitors the position of employers participating in the Fund, particularly those which may be susceptible to the events outlined, and takes advice from the Fund Actuary when required.

In addition, the administering authority keeps in close touch with all individual employers participating in the Fund to ensure that, as administering authority, it has the most up to date information available on individual employer situations. It also keeps individual employers briefed on funding and related issues.

Governance risks

Accurate data is necessary to ensure that members ultimately receive their correct benefits. The administering authority is responsible for keeping data up to date and results of the actuarial valuation depend on accurate data. If incorrect data is valued then there is a risk that the contributions paid are not adequate to cover the cost of the benefits accrued.

Monitoring and review

This FSS is reviewed formally, in consultation with the key parties, at least every three years to tie in with the triennial actuarial valuation process.

The most recent valuation was carried out as at 31 March 2019, certifying the contribution rates payable by each employer in the Fund for the period from 1 April 2020 to 31 March 2023.

The timing of the next funding valuation is due to be confirmed as part of the government's *Local government pension scheme: changes to the local valuation cycle and management of employer risk* consultation which closed on 31 July 2019. At the time of drafting this FSS, it is anticipated that the next funding valuation will be due as at 31 March 2022 but the period for which contributions will be certified remains unconfirmed.

The administering authority also monitors the financial position of the Fund between actuarial valuations and may review the FSS more frequently if necessary.

Approved by the Pensions Committee
Somerset County Council Pension Fund
XXXXXXXXXXX

Appendix A

Somerset County Council Pension Fund Contribution Review Policy

Contents

Introduction

This document sets out the Somerset County Council Pension Fund’s policy on amending the contribution rates payable by an employer (or group of employers) between formal funding valuations.

Somerset County Council Pension Fund (the Fund) is part of the Local Government Pension Scheme (LGPS), a defined benefit statutory scheme administered in accordance with the Local Government Pension Scheme Regulations 2013 (the Regulations) as amended.

Under Regulation 62, Somerset County Council, as the administering authority for the Fund, is required to obtain a formal actuarial valuation of the Fund and a rates and adjustments certificate setting out the contribution rates payable by each Scheme employer for three year period beginning 1 April following that in which the valuation date falls.

It is anticipated for most Scheme employers that the contribution rates certified at the formal actuarial valuation will remain payable for the period of the rates and adjustments certificate. However, there may be circumstances where a review of the contribution rates payable by an employer (or a group of employers) under Regulation 64A is deemed appropriate by the administering authority. This policy document sets out the administering authority’s approach to considering the appropriateness of a review and the process in which a review will be conducted.

This policy has been prepared by the administering authority following advice from the Fund Actuary, and following consultation with the Fund’s Scheme employers. In drafting this policy document, the administering authority has taken into consideration the statutory guidance on drafting a contribution review policy which was issued by the Ministry of Housing, Communities and Local Government, and the Scheme Advisory Board’s guide to employer flexibilities.

Throughout this document, any reference to the review of a Scheme employer’s contribution rates will also mean the single review of the contribution rates for a group of Scheme employers (for example if the employers are pooled for funding purposes).

Note that where a Scheme employer seems likely to exit the Fund before the next actuarial valuation then the administering authority can exercise its powers under Regulation 64(4) to carry out a review of contributions with a view to providing that assets attributable to the Scheme employer are equivalent to the exit payment that will be due from the Scheme employer. These cases do not fall under this contribution review policy.

The review process

The events that may trigger a review are set out in the Triggering a contribution review section. The general process for assessing and conducting a review is set out below. Timescales may vary in practice depending on each individual circumstance but the timeline below provides a rough guide of the administering authority's general expectation.

Following completion of the review process, the administering authority may continue to monitor the Scheme employer's position in order to ensure the revised contribution rate remains appropriate (where a review was completed) or to ensure the Scheme employer's situation does not change such that a review previously deemed not appropriate becomes appropriate. As part of its participation in the Fund, any Scheme employer is expected to support any reasonable information requests made by the administering authority in order to allow effective monitoring.

Timeline where initiation is made by the administering authority

Where the review is initiated by the administering authority (i.e. under conditions (i) and (ii) in the Triggering a contribution review section), the first stage after the administering authority has conducted its analysis is to engage with the Scheme employer and provide written evidence for requiring the review.

The Scheme employer will be given 28 days from the later of the date of receipt of the evidence provided by the administering authority and the date of receipt of the results of the formal contribution review to respond to the administering authority on the proposal. Should no challenge be accepted within this period then the administering authority will treat the proposal as accepted and the revised contribution rates will come into effect from the proposed review date.

Should the Scheme employer challenge the administering authority's proposal, then the administering authority will continue to engage with the Scheme employer in order to reach an agreeable decision. If no decision has been agreed within 3 months of the initial proposal, then the administering authority may proceed with the revised contribution rates. Further details of the appeals process for the Scheme employer is set out in the Appeals process section.

Although the ultimate decision for review belongs to the administering authority, the administering authority is committed to engaging with any Scheme employer following the initial proposal to ensure that any change is agreeable to all relevant parties.

Timeline where initiation is made by the Scheme employer

Where the review is initiated by the Scheme employer, the process begins once the Scheme employer has provided all the relevant documents required as set out in the Triggering a contribution review section.

The administering authority will aim to provide a response to the Scheme employer within 28 days from the date of receipt. This will depend on the quality of the documents provided and any need from the administering authority to request further information from the Scheme employer. The administering authority will provide a written response setting out the issues considered in reviewing the request from the Scheme employer, together with the outcome and confirming the next steps in the process.

Responsibility of costs

Where the review of contributions has been initiated by the administering authority, any costs incurred as part of the review in relation to the gathering of evidence to present to the Scheme employer and the actuarial costs to commission the contribution review will be met by the Fund. This is with the exception of any costs incurred as a result of extra information requested by the Scheme employer which is not ordinarily anticipated to be incurred by the administering authority as part of the review. These exception costs would be recharged to the Scheme employer.

Any costs incurred as a result of a review initiated by the Scheme employer will be the responsibility of the Scheme employer, regardless of the outcome of the review proceeding or not. This may include specialist adviser costs involved in assessing whether or not the request for review should be accepted and the costs in relation to carrying out the review.

Triggering a contribution review

As set out in Regulation 64(A)(1)(b), a review of an employer's contribution rate between formal actuarial valuations may only take place if one of the following conditions are met:

(i) it appears likely to the administering authority that the amount of the liabilities arising or likely to arise has changed significantly since the last valuation;

(ii) it appears likely to the administering authority that there has been a significant change in the ability of the Scheme employer or employers to meet the obligations of employers in the Scheme; or

(iii) a Scheme employer or employers have requested a review of Scheme employer contributions and have undertaken to meet the costs of that review.

Conditions (i) and (ii) are triggered by the administering authority and (iii) by the Scheme employer. The key considerations under each of the conditions are detailed below.

It should be noted that the conditions are as set out in the Regulations therefore do not allow for a review of contributions where the trigger is due to a change in actuarial assumptions or asset values.

(i) change in the amount of the liabilities arising or likely to arise

Examples of changes which may trigger a review under this condition include, but are not limited to:

- Restructuring of a council due to a move to unitary status
- Restructuring of a Multi Academy Trust
- A significant outsourcing or transfer of staff
- Any other restructuring or event which could materially affect the Scheme employer's membership
- Changes to whether a Scheme employer is open or closed to new members, or a decision which will restrict the Scheme employer's active membership in the fund in future
- Significant changes to the membership of an employer, for example due to redundancies, significant salary awards, ill health retirements or a large number of withdrawals
- Establishment of a wholly owned company by a scheduled body which does not participate in the LGPS.

As part of its participation in the Fund, Scheme employers are required to inform the administering authority of any notifiable events as set out in the Fund's Pensions Administration Strategy, service agreements and/or admission agreements. Through this notification process, the administering authority may identify events that merit a review of contributions.

In addition, the administering authority may initiate a review of contributions if they become aware of any events that they deem could potentially change the liabilities of the Scheme employer. This also applies to any employers for whom a review of contributions has already taken place as a further change in liabilities may merit another review.

(ii) change in the ability of the Scheme employer to meet its obligations

Examples of changes which may trigger a review under this condition include, but are not limited to:

- Change in employer legal status or constitution
- Provision of, or removal of, security, bond, guarantee or some other form of indemnity by a Scheme employer
- A change in a Scheme employer's immediate financial strength
- A change in a Scheme employer's longer-term financial outlook
- Confirmation of wrongful trading
- Conviction of senior personnel
- Decision to cease business
- Breach of banking covenant
- Concerns felt by the administering authority due to behaviour by a Scheme employer's, for example, a persistent failure to pay contributions (at all, or on time), or to reasonably engage with the administering authority over a significant period of time.

The administering authority is committed to engaging with Scheme employers on their participation in the Fund and through this can identify any Scheme employers that might be considered as high risk and whether any Scheme employers have had a significant change in riskiness. This in turn may affect the administering authority's views on whether the ability of a Scheme employer to meet its obligations to the Fund has changed significantly and therefore whether this change may merit a contribution review. This also applies to any employers for whom a review of contributions has already taken place as a further change in an employer's ability to meet its obligations may merit another review.

(iii) request from the Scheme employer for a contribution review

A request can be made by a Scheme employer for a review of contribution rates outside of the formal actuarial process. This must be triggered by one of the following two conditions:

- There has been a significant change in the liabilities arising or likely to arise; and/or
- There has been a significant change in the ability of the Scheme employer to meet its obligations to the Fund.

Any requests not arising from either of these conditions will not be considered by the administering authority.

Requests by a Scheme employer are limited to one review per calendar year.

With the exception of any cases where the Scheme employer is expected to cease before the next rates and adjustments certificate comes into effect, the administering authority will not accept a request for a review of contributions with an effective date within the 12 months preceding the next rates and adjustments certificate. It is expected in these cases that any requests can be factored in to the formal review and any benefits of carrying out a review just prior to the commencement of a new rates and adjustments certificate are outweighed by the costs and resource required. If a request is made with an effective date within the 12 months preceding the next rates and adjustments certificate, the administering authority will instead reflect these changes in the actuarial valuation and the rates being certified and taking effect the year following the valuation date.

Information required from the Scheme employer

In order to submit a request for a review of contribution rates outside of the formal actuarial valuation process, a Scheme employer must provide the following to the Fund:

- Where a review is sought due to a potential change in the Scheme employer's liabilities:
- Membership data or details of membership changes to evidence that the liabilities have materially changed, or are likely to change
- Where a review is sought due to a potential change in the ability of the Scheme employer to meet its obligations:
    - The most recent annual report and accounts for the Scheme employer
    - The most recent management accounts
    - Financial forecasts for a minimum of three years
    - The change in security or guarantee to be provided in respect of the Scheme employer's liabilities

The administering authority may require further evidence to support the request and this will be requested from the Scheme employer on a case by case basis.

Assessing the appropriateness of a review

The following general considerations will be taken into account by the administering authority, regardless of the condition under which a review is requested:

- the expected term for which the Scheme employer will continue to participate in the Fund;
- the time remaining to the next formal funding valuation;
- the cost of the review relative to the anticipated change in contribution rates and the benefit to the Scheme employer, the Fund and/or the other Scheme employers; and
- the anticipated impact on the Fund and the other Fund employers, including the relative size of the change in liabilities and contributions and any change in the risk borne by other Fund employers.

Where the review has been requested by the Scheme employer, the administering authority will also consider the information and evidence put forward by the Scheme employer. This may be with advice from the Fund Actuary where required, and will include an assessment of whether there is a reasonable likelihood that a review would result in a change in the Scheme employer's contribution rates. The administering authority will also consider whether it is necessary to consult with any other Scheme employer e.g. where a guarantee may have been provided by another Scheme employer.

Whether any changes require the administering authority to exercise its powers to carry out a contribution review will be assessed on a case by case basis and with advice from the Fund Actuary and may involve other considerations as deemed appropriate for the situation. The final decision of whether a review of contribution rates will be carried out rests with the administering authority after, if necessary, taking advice from the Fund Actuary. Should a Scheme employer disagree with the administering authority, then details of the Appeals process is set out later in this document.

Appropriateness of a review due to change in liabilities

This will be subject to the following considerations in addition to the general considerations set out above:

- the size of the Scheme employer's liabilities relative to the Fund and the extent to which they have changed;
- the size of the event in terms of membership and liabilities relative to the Scheme employer and/or the Fund; and
- the administering authority's assessment of the ability of the Scheme employer to meet its obligations.

Appropriateness of a review due to change in ability to meet its obligations to the Fund

In assessing whether or not an administering authority will exercise its powers to review a Scheme employer's contribution rates under this condition, the administering authority will take into account the general considerations set out earlier in this section and:

- The results of any employer risk analysis provided by the Fund Actuary or a covenant specialist
- The perceived change in the value of the indemnity to the administering authority, relative to the size of the Scheme employer's liabilities

It is acknowledged that each Scheme employer's situation may differ and therefore each decision will be made on a case by case basis. Further considerations to that set out above may be relevant and will be taken into account by the administering authority as required.

Method used for reviewing contribution rates

If a review of contribution rates is agreed, or if an indicative review is required to help inform the review process, the administering authority will take advice from the Fund Actuary on the calculation of the Scheme employer's revised contribution rates. This will take into account the events leading to the anticipated liability change and any impact of the changes in the Scheme employer's ability to meet its obligations to the Fund.

The starting point for reviewing a Scheme employer's contribution rates will in some cases be the most recent actuarial valuation. The table below sets out the general approach that will be used when carrying out this review.

Once a review of contribution rates has been agreed, unless the impact of amending the contribution rates is deemed immaterial by the Fund Actuary, then the results of the review will be applied with effect from the agreed review date.

	General approach
Member data	In some cases, where the review is happening during or shortly after the valuation, the most recent actuarial valuation data will be used as a starting point. In most cases, given the review is due to an anticipated change in membership, the administering authority and Scheme employer should work together to provide updated membership data for use in calculations. There may be instances where updated membership data is not required if it is deemed proportionate to use the most recent actuarial valuation data without adjustment. Where the cause for a review is due to a change in a Scheme employer's ability to meet its obligations to the Fund, updated membership data may not need to be used unless any significant membership movements since the previous Fund valuation are known.

	General approach
Approach to setting assumptions	This will be in line with that adopted for the most recent actuarial valuation, and in line with that set out in the Fund's Funding Strategy Statement.
Market conditions underlying financial assumptions	Unless an update is deemed more appropriate by the Fund Actuary, the market conditions will be in line with those at the most recent actuarial valuation.
Conditions underlying demographic assumptions	Unless an update is deemed more appropriate by the Fund Actuary, the conditions will be in line with those at the most recent actuarial valuation.
Funding target	The funding target adopted for a Scheme employer will be set in line with the Fund's Funding Strategy Statement, which may be different from the approach adopted at the most recent actuarial valuation due to a change in the Scheme employer's circumstances.
Surplus/deficit recovery period	The surplus/deficit recovery period adopted for a Scheme employer will be set in line with the Fund's Funding Strategy Statement, which may be different from the approach adopted at the most recent actuarial valuation due to a change in the Scheme employer's circumstances.

The Fund Actuary will be consulted throughout the review process and will be responsible for providing revised rates and adjustments certificate. Any deviations from the general approaches set out above will be agreed by the administering authority and the Fund Actuary.

Appeals process

Whether a contribution review is agreed or not is ultimately the decision of the administering authority. In the event of any dispute from the employer, the Fund will allow an additional 21 days for further discussion with the employer to seek to resolve the issues raised. Employers are also entitled to raise any concerns direct to the Pension Board, via one of the Board's employer representatives.

Approved by the Pensions Committee
Somerset County Council Pension Fund
XXXXXXXXXXX

Appendix A

Somerset County Council Pension Fund Deferred Debt and Debt Spreading Agreements Policy

Contents

Introduction

This document sets out the Somerset County Council Pension Fund's policy on deferred debt agreements (DDAs) and debt spreading agreements (DSAs) for exiting employers.

Somerset County Council Pension Fund (the Fund) is part of the Local Government Pension Scheme (LGPS), a defined benefit statutory scheme administered in accordance with the Local Government Pension Scheme Regulations 2013 (the Regulations) as amended.

When a Scheme employer becomes an exiting employer under Regulation 64, the Fund Actuary is required to carry out a valuation to determine the exit payment due from the exiting employer to the Fund, or the excess of assets in the Fund relating to that employer. Where an exit payment is due, the expectation is that the employer settles this debt immediately through a single cash payment. However, if the employer provides evidence that this is not possible, there are two alternatives available: Regulation 64(7A) enables the administering authority to enter into a deferred debt agreement with the employer while Regulation 64B enables the administering authority to enter into a debt spreading agreement.

Under a DDA, the exiting employer becomes a deferred employer in the Fund (i.e. they remain as a Scheme employer but with no active members) and remains responsible for paying any existing or future secondary rate of contributions to fund any current or future deficit. The secondary rate of contributions will be reviewed at each actuarial valuation until the termination of the agreement.

Under a DSA, the cessation debt is crystallised and spread, with interest, over a period deemed reasonable by the administering authority having regard to the views of the Fund Actuary.

Whilst a DSA involves crystallising the cessation debt and the employer's only obligation is to settle this set amount, in a DDA the employer remains in the Fund as a Scheme employer and is exposed to the same risks (unless agreed otherwise with the administering authority) as active employers in the Fund (e.g. investment, interest rate, inflation, longevity and regulatory risks) meaning that the deficit will change over time.

This policy document sets out the administering authority's policy for entering into, monitoring and terminating a DDA or DSA.

These policies have been prepared by the administering authority following advice from the Fund Actuary, and following consultation with the Fund's Scheme employers. In drafting this policy document, the administering authority has taken into consideration the statutory guidance on preparing and maintaining policies on employer exit payments and deferred debt agreements which was issued by the Ministry of Housing, Communities and Local Government, and the Scheme Advisory Board's guide to employer flexibilities.

Approach for exiting employers

In the event that an employer becomes an exiting employer and an exit payment is identified, the Fund should seek to receive a payment from the exiting employer equal to the exit payment in full.

The administering authority makes the exiting employer aware an exit payment is due by providing a revised rates and adjustments certificate in the form of a cessation valuation report produced by the Fund Actuary. Details of the Fund's cessation policy can be found in the Fund's FSS.

The default position is that the employer is required to make an exit payment in full immediately. However, if required, the exiting employer can inform the administering authority, along with evidence, that they are unable to do so and may request to enter either a DDA or DSA. If the administering authority is satisfied with the evidence provided, the DDA or DSA process may proceed.

Requests should be submitted within 21 days of receiving confirmation of the exit payment required, or otherwise the exit payment should be paid to the Fund in full within 28 days.

Where possible, the administering authority encourages employers who are approaching exit and suspect they will have a deficit to engage with the administering authority in advance in order to understand the options that may be available. An indicative cessation report can be produced to form the basis of discussions.

Choosing a DDA or DSA

Consideration needs to be given as to which approach is the most appropriate in each case. A DDA may be appropriate if:

- the employer temporarily has no active members but expects it may return to active employer status in future. However, please note that if the plan is for active members to join within three years then perhaps a suspension notice may be more appropriate;
- the employer wants to minimise costs by potentially benefitting from the upside of the pensions risks it would remain exposed to and therefore does not want to crystallise its debt by becoming an exiting employer. In this case the administering authority may be willing to defer crystallisation of the cessation debt for an appropriately significant period of time, subject to the strength of the employer's covenant or security provided;
- initial affordability of the full exit payment is low but there is a prospect of increased affordability in the future, or the payment can only be afforded over a long period and therefore a DDA enables the position to be updated over time in light of changing funding positions; and/or
- the employer has a weak covenant but is not faced with imminent insolvency and must rely on future investment returns to fully or partially fund the exit payment. The administering authority may agree that doing so over an appropriate long period is better for the Fund than risking immediate insolvency of the employer.

On the other hand, it may be more appropriate to enter a DSA if:

- the employer does not intend to employ any more active members and therefore is not expected to resume active employer status;
- the employer wishes to crystallise its debt to the Fund and therefore not be subject to any of the pensions risks that could cause the amounts payable to the Fund increasing (or decreasing) in future;
- the employer has ample resources to make the payment within the near future but not immediately; and/or
- the employer is deemed to have a very weak covenant and so the administering authority will want to try to recoup as much of the exit payment as possible before the employer becomes insolvent.

The administering authority has the right to refuse a DSA or DDA request if they believe it is not in the best interests of the Fund or the other participating employers, for example if entering a DSA or DDA increases the risk of a deficit falling to the other employers.

In considering each request for a DDA or DSA arrangement from an exiting employer the administering authority will take actuarial, covenant, legal and other advice as necessary. Proposed DDAs/DSAs will always be discussed with the employer, whether the arrangement was at the exiting employer's request or not.

Employers who may be party to either a DSA or a DDA are encouraged to discuss any potential impact on their accounting treatment with their auditors.

Managing of costs

On receiving a request the administering authority will make the employer aware that any costs associated with setting up the DDA or DSA will be the responsibility of the Scheme employer, regardless of whether the administering authority agrees to enter into the agreement or not. This may include the cost of actuarial advice, legal advice, administrative costs and any additional advice required in relation to a covenant assessment or any other specialist adviser costs. If costs deviate from those initially anticipated the administering authority will keep the exiting employer up-to-date with any increases. The administering authority will provide information on how and when payments should be made.

Appeals process

Whether a DDA or DSA arrangement is agreed or not is ultimately the decision of the administering authority. In the event of any dispute from the employer, the Fund will allow an additional 21 days for further discussion with the employer to seek to resolve the issues raised. Employers are also entitled to raise any concerns direct to the Pension Board, via one of the Board's employer representatives.

Deferred Debt Agreements (DDAs)

Entering into a DDA

Under a DDA, the exiting employer becomes a deferred employer in the Fund (i.e. they remain as a Scheme employer but with no active members) and remains responsible for paying the secondary rate of contributions to fund their deficit.

Information required from the employer

When making a request to enter a DDA, the employer should demonstrate that they are unable to settle their exit payment immediately and provide any relevant information to support their request e.g. in relation to their covenant/ability to continue to make payments to the Fund on a continuing basis. Examples of information the employer may provide as evidence include the exiting employer's:

- most recent annual report and accounts
- latest management accounts
- financial forecasts
- details of position of other creditors

This is not an exhaustive list and the administering authority may request further evidence. In particular, the administering authority may commission a covenant assessment if insufficient evidence is provided.

Assessing the proposal

The administering authority will make a decision on whether to enter into a DDA within 21 days of receiving a request but this may vary to reflect specific circumstances, for example if the administering authority chooses to request a covenant assessment then the process may take longer.

To reach a decision the administering authority will consider:

- the size of the exiting employer's residual liabilities relative to the size of the Fund;
- the size of the exit payment relative to the costs associated with entering into a DDA;
- whether a debt spreading agreement or suspension notice would be more appropriate (see specific circumstances below);
- any information provided by the exiting employer to support their covenant strength, including any information on a guarantor or other form of security that the employer may be able to put forward to support their covenant;
- the results of any covenant review carried out by the Fund Actuary or a covenant specialist;
- the exiting employer's accounts;
- the potential impact on the other employers in the Fund; and
- the opinion of the Fund Actuary.

The administering authority is not obliged to accept an exiting employer's request for a DDA. For example, in the following circumstances the administering authority may consider a DDA not to be appropriate:

- the exiting employer could reasonably be expected to settle their exit payment in a single amount;
- it is known or likely that another active member will come into employment in the three years following the cessation date (in these cases a suspension notice would be considered more appropriate than a DDA); or
- the administering authority is concerned that where a DDA is entered, that the employer could not afford the impact of any negative experience which would result in an increase in the required secondary rate of contributions and an increase in the employer's overall deficit (in these cases a debt spreading agreement would be considered more appropriate as the payments are fixed throughout the term of the agreement).

Once all information has been considered the administering authority will consult with the exiting employer as required under the Regulations. If the administering authority does not wish to enter into a DDA they will explain to the exiting employer their reasoning and any alternatives (e.g. a debt spreading agreement, suspension notice or indeed require the exit payment in full). If the administering authority accepts the request to enter into a DDA, they will notify their legal advisers and Fund Actuary. If the administering authority has concerns about the level of risk arising due to the DDA, the administering authority may only accept the request subject to a one-off cash injection being made by the exiting employer or security being provided as an additional guarantee.

Setting up a DDA

Once agreed that a DDA is permitted, the terms of the DDA will be agreed between the administering authority and the exiting employer and will be set out in a formal legal agreement.

The administering authority and the exiting employer (with the assistance of the Fund Actuary) will negotiate an appropriate duration of the agreement which will consider the exiting employer's affordability and anticipated strength of covenant over the agreement period. If the exiting employer has sufficient reserves, the administering authority may require an immediate cash payment so that the DDA can start from an acceptably stronger funding position.

The Fund Actuary will calculate secondary contributions on an appropriate basis as agreed with the administering authority and following consultation with the exiting employer, taking into account any cash payments made in advance. The secondary contributions will be reviewed at each actuarial valuation and certified as part of the Fund's Rates and Adjustments Certificate until the termination of the agreement. Therefore payments throughout the agreement are not known in advance and may increase or decrease at each valuation to reflect changes in the employer's funding position.

The timeline from consultation with the exiting employer to entering into a DDA to the signing of the agreement will vary. Where possible all parties will aim to have the agreement signed within 3 months, although there may be circumstances where timings may vary.

Once finalised, the employer will become a deferred employer in the Fund and will have an obligation to pay their secondary contributions as certified by the Fund Actuary. The responsibilities of the deferred employer will be set out in the legal agreement and these will include the requirements to:

- comply with all the requirements on Scheme employers under the Regulations except the requirement to pay a primary rate of contributions but including any additional applicable costs, such as strain costs as a result of ill health retirements;
- adopt the relevant practices and procedures relating to the operation of the Scheme and the Fund as set out in any employer's guide produced by the administering authority;
- comply with all applicable requirements of data protection law relating to the Scheme and with the provisions of any data-sharing protocol produced by the administering authority and provided to the deferred employer;
- promptly provide all such information that the administering authority may reasonably request in order to administer and manage the agreement; and
- give notice to the administering authority, of any actual or proposed change in its status, including take-over, change of control, reconstruction, amalgamation, insolvency, winding up, liquidation or receivership or a material change to its business or constitution.

The deferred employer should consult with their auditors about any impacts the DDA is expected to have on their accounting requirements.

Monitoring a DDA

A deferred debt agreement is subject to the ongoing approval of the administering authority. The administering authority reserves the right to terminate the agreement should they become concerned about a significant weakening in the deferred employer's covenant or a significant change in funding position. Conversely, if there was an improvement in the employer's circumstance then the administering authority and employer may agree to amend the terms of the agreement.
The administering authority will monitor a DDA in the following ways:

Change in funding position

The administering authority will request regular, and at least annual, updates of the deferred employer's funding position in order to review the progress of the DDA. The costs of the regular reviews will fall to the deferred employer as part of the terms for putting in place a DDA.
If the funding position changes by more than 10% (in absolute terms) from the previous review then the administering authority may engage with the deferred employer to discuss a possible review of the DDA.

Change in employer covenant

Once an employer enters into a DDA, the administering authority will review the employer's covenant on a regular basis and details of this will be agreed for each DDA on an individual basis. If a deferred employer's covenant deteriorates, the administering authority may issue a notice to review and possibly terminate the agreements.

In addition, if a deferred employer requests an extension to the duration of the DDA the administering authority will consider an updated covenant review, amongst other factors, in assessing the proposal.

As a condition of entering into a DDA, the deferred employer is required to engage with the administering authority to assist with monitoring the level of covenant, for example by providing information requested by the administering authority in a timely manner.

Timeliness of payments

The agreement will set out whether payments are made on a monthly or annual basis, and the administering authority will monitor if contributions are paid on time. Successive late or in particular missing payments would contribute towards a notice being issued to the deferred employer to review and possibly terminate the agreement.

Strength of guarantee or security

If a particular funding basis has been used by the Fund Actuary on the understanding that there is a particular security in place (e.g. another employer in the Fund willing to underwrite the residual deferred and pensioner liabilities when the employer formally exits) then the administering authority will check there has been no change to the security at agreed regular intervals and as a minimum at each valuation cycle. The Fund Actuary may change the funding basis used to set the deferred employer's contributions depending on the strength of the security in place.

Notifiable events from the deferred employer

The deferred employer has a responsibility to make the administering authority aware of any changes in their ability to make payments or of a change in circumstance (e.g. a change of the guarantee in place mentioned above). Information should be shared with the administering authority at any time throughout the agreement to enable the administering authority to consider whether a review of the agreement should be carried out.

Terminating a DDA

Events that may terminate a DDA

As set out in Regulation 64(7E), the DDA terminates on the first of the following events:

- the deferred employer enrols new active members;
- the duration of the agreement has elapsed;
- the take-over, amalgamation, insolvency, winding up or liquidation of the deferred employer;
- the administering authority serves a notice on the deferred employer that it is reasonably satisfied that the employer's ability to meet the contributions payable under the DDA has weakened materially (or is likely to in the next 12 months); or
- a review of the funding position of the deferred employer is carried out at an updated calculation date and the Fund Actuary assesses that the deferred employer has paid sufficient secondary contributions to cover what would be due if the deferred employer terminated at the updated calculation date; in other words the review reveals no deficit remains on the relevant calculation basis.

The deferred employer can also choose to terminate the DDA at any point. Notice should be given to the administering authority at the earliest opportunity. Termination clauses will be included in the formal DDA legal agreement.

Process of termination

Once a termination of the DDA has been triggered, the deferred employer becomes an exiting employer under Regulation 64(1). The administering authority will obtain from the Fund Actuary an exit valuation calculated at the date the DDA terminates, and a revised rates and adjustments certificate setting out the exit payment due from the exiting employer or the excess of assets in the Fund relating to the exiting employer (which would then be subject to the Fund's exit credit policy).

Once the exit payment has been made in full, the exiting employer has no further obligation to the Fund.

If the termination has been triggered because the deferred employer has enrolled new active members then the deferred employer becomes an active employer in the Fund and an immediate exit payment may not be required; this may instead be incorporated in the revised rates and adjustments certificate that will be provided in respect of the active employer. The employer remains responsible for all previously accrued liabilities and the revised contributions required from the active employer will be calculated in line with the Fund's Funding Strategy Statement (FSS).

If the termination has been triggered because a review of the funding position of the deferred employer reveals that the secondary contributions paid to date by the deferred employer are sufficient to cover what would be due if the deferred employer terminated at the updated calculation date, then the deferred employer becomes an exiting employer and no further payments are required. The exiting employer has no further obligation to the Fund. Where there is a surplus, an exit credit may be payable as determined by the administering authority and in line with the Fund's exit credit policy.

Debt Spreading Agreements (DSAs)

Entering a DSA

Under a DSA, the cessation debt is crystallised and spread, with interest, over a period deemed reasonable by the administering authority having regard to the views of the Fund Actuary and following discussion with the exiting employer. The payments are fixed and are not reviewed at each actuarial valuation.

Information required from the employer

When making a request to enter a DSA, the exiting employer should demonstrate that they are unable to settle their exit payment immediately and provide any relevant information to support their request e.g. in relation to their covenant/ability to continue to make payments to the Fund. Examples of information the exiting employer may provide as evidence include the employer's:

- most recent annual report and accounts
- latest management accounts
- financial forecasts
- details of position of other creditors

This is not an exhaustive list and the administering authority may request further evidence. In particular, the administering authority may commission a covenant assessment if insufficient evidence is provided.

Assessing the proposal

The administering authority will make a decision on whether to enter into a DSA within 28 days of receiving a request but this may vary to reflect specific circumstances, for example if the administering authority chooses to request a covenant assessment then the process may take longer.

To reach a decision the administering authority will consider:

- the size of the exit payment relative to the exiting employer's business cashflow;
- the size of the exit payment relative to the costs associated with entering into a DSA;
- whether a deferred debt agreement or suspension notice would be more appropriate;
- any information provided by the employer to support their covenant strength;
- the results of any covenant review carried out by the Fund Actuary or a covenant specialist;
- the merit of any guarantees from another source and whether this is deemed sufficient to cover the outstanding payments should the exiting employer fail;
- the exiting employer's accounts;
- the potential impact on the other employers in the Fund; and
- the opinion of the Fund Actuary.

The administering authority is not obliged to accept an exiting employer's request for a DSA. For example, in the following circumstances the administering authority may consider a DSA not to be appropriate:

- the exiting employer could reasonably be expected to settle their exit payment in a single amount;
- there is doubt that the exiting employer can operate as a going concern during the spreading period; or
- the exiting employer cannot afford the speeded payments over the maximum spreading period or is requesting a spreading period longer than the maximum (see below).

The structure of the DSA is at the discretion of the administering authority having taken advice from the Fund Actuary and consulted with the exiting employer. The structure should protect all other employers in the Fund whilst being achievable for the exiting employer. The structure of the DSA will take into consideration:

- the period that the payments will be spread. This is expected to be no more than 5 years. For longer periods it may be more appropriate to consider a deferred debt agreement but the administering authority reserves the right to set whatever spreading period they deem appropriate provided they are satisfied with the exiting employer's ability to meet the payments over that period. The length of the spreading period will be set as to be as short as possible whilst remaining affordable for the exiting employer;
- the interest rate applicable to the spread payments. In general, this will be set with reference to the discount rate in the employer's cessation valuation, for consistency with the liabilities calculated;
- the regularity of the payments and when they fall due;
- other costs payable; and
- the responsibilities of the exiting employer during the spreading period (for example, to make payments on time and to notify the administering authority of a change in circumstances that could affect their ability to make payments).

Once all information has been considered the administering authority will consult with the exiting employer as required under the Regulations. If the administering authority does not wish to accept the exiting employer's request to enter into a DSA they will explain their reasoning and any alternatives (e.g. a DDA, suspension notice or indeed require the exit payment in full). If the administering authority accepts the request to enter into a DSA, they will notify their legal advisers and Fund Actuary. If the administering authority has concerns about the level of risk arising due to the DSA, the administering authority may only accept the request subject to a one-off cash injection being made by the exiting employer or security being provided as an additional guarantee.

Setting up a DSA

The administering authority and the exiting employer, with the assistance of the Fund Actuary, will then negotiate the structure of the schedule of payments which takes into consideration the exiting employer's affordability and an appropriate period of the spreading.

The schedule of payments will be set out in a revised rates and adjustments certificate prepared by the Fund Actuary. There may be circumstances where timings may vary, however, in general the certificate will be prepared and provided to the exiting employer within 28 days of agreeing the structure of the schedule of payments with the exiting employer.

Monitoring a DSA

Over the term that the cessation debt payment is spread, the administering authority will monitor the ability and willingness of the exiting employer to pay the schedule of contributions in the revised rates and adjustments certificate. While it is expected the schedule of payments would be fixed for the spreading period, the administering authority may alter the structure of the schedule at any time if there is a change in the exiting employer's circumstances or indeed, if the exiting employer wanted to pay the remaining balance. This will be agreed on a case by case basis and set out in a side agreement as required.

The administering authority will be in regular contact with the exiting employer until their obligations to the Fund are removed when all payments set out in the schedule of payments are made.

Examples of factors which will be monitored are set out below. Should any of these raise any concerns with the administering authority then the DSA may be reviewed and/or terminated.

<u>Change in employer covenant</u>

The administering authority will monitor the ability of the exiting employer to make their set payments by monitoring publicly available information such as credit ratings and/or company accounts as well as keeping in regular contact, at least annually, with the exiting employer to ensure that the payments can be met.

As a condition of entering into a DSA, the exiting employer is required to engage with the administering authority to assist with monitoring the level of covenant, for example by providing information requested by the administering authority in a timely manner.

<u>Timeliness of payments</u>

The DSA will set out whether payments are made on a monthly or annual basis and how long for, and the administering authority will monitor if contributions are paid on time. Successive late or in particular missing payments would contribute towards further interest charges or the spreading agreement may be reviewed and/or terminated.

Strength of guarantee or security

If a particular schedule of payments has been agreed between the administering authority and the exiting employer on the understanding that there is a particular security in place (e.g. another employer in the Fund willing to pay the remaining balance or a fixed charge on property that covers the remaining balance) then the administering authority will check there has been no change to the security regularly. The frequency of these reviews may reduce as the level of outstanding debt reduces. The administering authority with advice from the Fund Actuary may change the schedule of payments depending on the strength of the security in place. The exiting employer would be consulted prior to any changes.

Notifiable events from the exiting employer

The exiting employer has a responsibility to make the administering authority aware of any changes in their ability to make payments or of a change in circumstance that affects their ability to make payments. Information should be shared with the administering authority at any time throughout the agreement to enable the administering authority to consider whether a review of the agreement should be carried out.

Terminating a DSA

Events that may terminate a DSA

On paying all the payments set out in the revised rates and adjustments certificate the exiting employer will no longer have any obligations to the Fund.

In the event that the administering authority believes that the exiting employer may not be able to make any of their remaining payments, the administering authority reserves the right to review and/or terminate the DSA to ensure it is appropriate for the Fund and does not adversely impact the other participating employers.

The exiting employer may also request to terminate the DSA early, in which case an immediate payment of the outstanding amounts set out in the contribution schedule should be paid.

Process of termination

In the event of a DSA being amended or terminated the administering authority will communicate this to the exiting employer along with reasons for the decision. Before the decision is made the administering authority will consult with the exiting employer about their change in circumstances and also take advice from the Fund Actuary.

If the DSA has to be terminated prematurely the administering authority will seek to obtain from the exiting employer as much of the outstanding exit payments as possible or look at alternative arrangements such as a deferred debt agreement. Once the exit payment has been made in full, the exiting employer has no further obligation to the Fund.

Approved by the Pensions Committee
Somerset County Council Pension Fund
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South Somerset District Council

2020/21 External Audit Plan

Executive Portfolio Holder:	Peter Seib, Finance and Legal Services
Director:	Nicola Hix, Support Services & Strategy
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Purpose of the Report

This report introduces Grant Thornton's Audit Plan for reviewing the Council's 2020/21 financial statements and our arrangements for securing value for money.

Public Interest

Under International Standards of Audit (UK) (ISAs) and the National Audit Office (NAO) Code of Audit Practice, the Council's external auditors report on the group and Council's financial statements and the governance of South Somerset District Council. The Audit plan provides an overview of the planned scope and timing of the statutory audit and the audit approach to be used in respect of the 2020/21 audit.

Recommendations

The Audit Committee is asked to note the Audit Plan for 2020/21.

Background

The Audit Plan is included within the remit of the Audit Committee under its terms of reference as follows:

"To consider and note the annual external Audit Plan and fees"

The attached plan provides an overview of the planned scope and timing of the statutory audit and the audit approach to be used in respect of the 2020/21 audit.

Financial Implications

The estimated fees outlined by Grant Thornton are £66,943 in respect of the statutory audit and £23,000 for the certification of the Housing Benefit claim making the estimated audit fee £89,943.

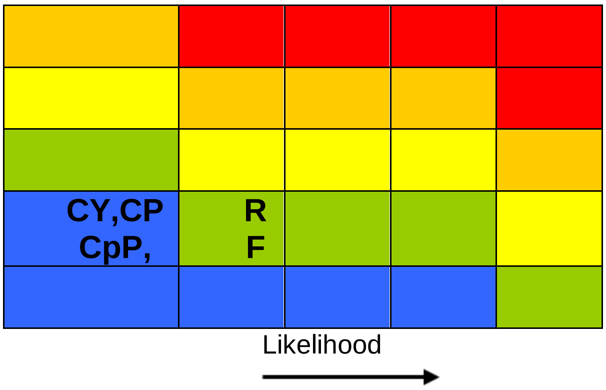
The approved budget is £60,250, if the fee continues to be at the 2020/21 level the additional budget pressure will be requested as part of the budget setting process.

South Somerset District Council

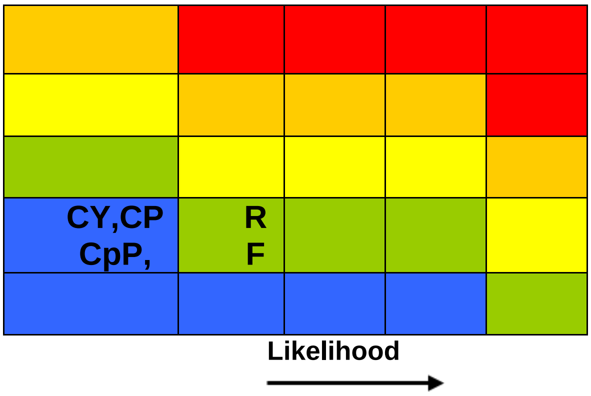
Officers will monitor the 2021/22 budgets in the service area to identify potential underspends which will be utilised to reduce the impact of this additional pressure.

Risk Matrix

Risk Profile before officer recommendations



Risk Profile after officer recommendations



Key

Categories	**Colours** (for further detail please refer to Risk management strategy)
R - Reputation	High impact and high probability
CpP - Corporate Plan Priorities	Major impact and major probability
CP - Community Priorities	Moderate impact and moderate probability
CY - Capacity	Minor impact and minor probability
F - Financial	Insignificant impact and insignificant probability

Council Plan Implications

There are no implications in approving this report

Carbon Emissions and Climate Change Implications

There are no implications in approving this report.

Equality and Diversity Implications

There are no implications in approving this report.

Privacy Impact Assessment

There is no personal information included in this report.

Background Papers

None

South Somerset District Council audit plan

Year ending 31 March 2021

South Somerset District Council

18 May 2021

Contents

Your key Grant Thornton team members are:

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The contents of this report relate only to the matters which have come to our attention, which we believe need to be reported to you as part of our audit planning process. It is not a comprehensive record of all the relevant matters, which may be subject to change, and in particular we cannot be held responsible to you for reporting all of the risks which may affect the Council or all weaknesses in your internal controls. This report has been prepared solely for your benefit and should not be quoted in whole or in part without our prior written consent. We do not accept any responsibility for any loss occasioned to any third party acting, or refraining from acting on the basis of the content of this report, as this report was not prepared for, nor intended for, any other purpose.

Key matters

Factors

Financial reporting and audit – raising the bar

The Financial Reporting Council (FRC) has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge, and to undertake more robust testing as detailed in Appendix 1.

Our work in 2019/20 highlighted areas where local government financial reporting, in particular, property, plant and equipment and pensions, needs to be improved, with a corresponding increase in audit procedures. We have also identified an increase in the complexity of local government financial transactions which require greater audit scrutiny.

Impact of Covid 19 pandemic

The outbreak of the Covid-19 coronavirus pandemic has had a significant impact on the normal operations of the Council and the financial forecast of the Council, particularly in the short term.

The Council has been supporting residents and business throughout the Covid-19 pandemic whilst delivering critical services. The Council administered various grants to businesses throughout the period including the Local restrictions Support Grant, Retail, Hospitality and Leisure Grant Funding and Small Business Grants.

The Council refreshed their 2020-21 budget in the second half of 2020 as the significant impact caused by the pandemic was not a major factor factor at the time the budget was approved in February 2020.

Due to the pressures faced by organisations in the public sector as a result of the pandemic, we are aware that there could be increased incentive and opportunity for the manipulation of organisations financial statements. As a result, we have identified an additional significant risk of fraud in relation to the 'fees and charges' element of the council's income from services.

Our response

- As a firm, we are absolutely committed to audit quality and financial reporting in the local government sector. Our proposed work and fee, as set further in our Audit Plan, has been discussed with the s151 Officer.
- We will consider your arrangements for managing and reporting your financial resources as part of our work in completing our Value for Money work.
- We will continue to provide you with sector updates via our Audit Committee updates.
- We have identified an increased incentive and opportunity for organisations in the public sector to manipulate their financial statements due to increasing financial pressures. We have identified a significant risk in regards to revenue recognition – refer to page 8.
- The Council's valuer reported a material uncertainty in regards to the valuation of properties in 2019/20 due to the Covid 19 pandemic and we expect significant uncertainty will continue in 2020/21. We identified a significant risk in regards to the valuation of properties – refer to page 7.

Introduction and headlines

Purpose

This document provides an overview of the planned scope and timing of the statutory audit of South Somerset District Council ('the Council') for those charged with governance.

Respective responsibilities

The National Audit Office ('the NAO') has issued a document entitled Code of Audit Practice ('the Code'). This summarises where the responsibilities of auditors begin and end and what is expected from the audited body. Our respective responsibilities are also set out in the agreed *the Terms of Appointment and Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA), the body responsible for appointing us as auditor of South Somerset District Borough Council.* We draw your attention to both of these documents.

Scope of our audit

The scope of our audit is set in accordance with the Code and International Standards on Auditing (ISAs) (UK).

We are responsible for forming and expressing an opinion on the Council and group's financial statements that have been prepared by management with the oversight of those charged with governance (the Audit committee).

We are also responsible for undertaking sufficient work to be able to satisfy ourselves as to whether the Council has appropriate arrangements for securing economy, efficiency and effectiveness in it's use of resources.

The audit of the financial statements does not relieve management or the Audit Committee of your responsibilities. It is the responsibility of the Council to ensure that proper arrangements are in place for the conduct of its business, and that public money is safeguarded and properly accounted for. We have considered how the Council is fulfilling these responsibilities.

Our audit approach is based on a thorough understanding of the Council's business and is risk based.

Group Audit

The Council is required to prepare group financial statements that consolidate the financial information of SSDC Opium Power Limited. SSDC Business Solutions Ltd. and Elleston Services Limited are excluded from consolidation on grounds of immateriality.

Significant risks

Those risks requiring special audit consideration and procedures to address the likelihood of a material financial statement error have been identified as:

- ISA 240- Revenue Risk (specifically including income from fees and charges)
- Management override of controls
- Valuation of land and buildings
- Valuation of Investment Properties
- Valuation of net pension fund liability

We will communicate significant findings on these areas as well as any other significant matters arising from the audit to you in our Audit Findings (ISA 260) Report.

Materiality

We have determined planning materiality to be £1.9m (PY £1.644m) for the group and £1.8m (PY 1.53m) for the Council, which equates to 2% of your gross expenditure for the year. We are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. Clearly trivial has been set at £0.91m (PY £0.75m).

Value for Money arrangements

Our risk assessment regarding your arrangements to secure value for money have identified no risks of significant weakness. We have identified a number of areas of focus at this time and these are detailed on page 16.

Audit logistics

Our interim work took take place in April and our final visit will take place in July to September. Our key deliverables are this Audit Plan, our Audit Findings Report and Auditor's Annual Report. Our audit approach is detailed in Appendix A.

Our fee for the audit will be £66,933 (PY: £69,759) for the Council, subject to the Council delivering a good set of financial statements and working papers.

Group audit scope and risk assessment

In accordance with ISA (UK) 600, as group auditor we are required to obtain sufficient appropriate audit evidence regarding the financial information of the components and the consolidation process to express an opinion on whether the group financial statements are prepared, in all material respects, in accordance with the applicable financial reporting framework.

Component	Individually Significant?	Level of response required under ISA (UK) 600	Risks identified	Planned audit approach
South Somerset District Council	Yes		Risks reported on pages 7 - 9	Full scope audit performed by Grant Thornton UK LLP
SSDC Opium Power Limited	Yes		Valuation of Property Plant & Equipment (as detailed on page 8) Management override of controls (as detailed on page 7)	Specific scope procedures on material group balances to be performed by Old Mill, as component auditor, with specific scope procedures to be performed by the Grant Thornton UK LLP audit team over the valuation of Property, Plant and Equipment. The nature, time and extent of our involvement in the work of Old Mill will begin with a discussion on risks, guidance on designing procedures, participation in meetings, followed by the review of relevant aspects of their audit documentation and meeting with appropriate members of management.

Audit scope

- Audit of the financial information of the component using component materiality
- Audit of one more classes of transactions, account balances or disclosures relating to significant risks of material misstatement of the group financial statements
- Review of component's financial information
- Specified audit procedures relating to significant risks of material misstatement of the group financial statements
- Analytical procedures at group level

Significant risks identified

Significant risks are defined by ISAs (UK) as risks that, in the judgement of the auditor, require special audit consideration. In identifying risks, audit teams consider the nature of the risk, the potential magnitude of misstatement, and its likelihood. Significant risks are those risks that have a higher risk of material misstatement.

Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
ISA240 revenue risk – the Council's reported revenue contains fraudulent transactions (partially rebutted)	Council & Group	Under ISA (UK) 240 there is a rebuttable presumed risk that revenue may be misstated due to the improper recognition of revenue. This presumption can be rebutted if the auditor concludes that there is no risk of material misstatement due to fraud relating to revenue recognition. For the group (excluding the Council), as revenue is immaterial, we have concluded we can rebut this risk, as group income is not material. For the Council we have concluded that the greatest risk of material misstatement relates to Fees & Charges income. We have therefore identified the accuracy and occurrence of Fees and Charges income (and associated receivable balances) as a significant risk, which is one of the most significant assessed risks of material misstatement. For the remaining revenue streams, we have rebutted this risk because: • other income streams are primarily derived from grants or formula-based income from central government and taxpayers; and • opportunities to manipulate revenue recognition are very limited.	Having considered the risk factors set out in ISA240 and the nature of the revenue streams at the Council, we have determined that the risk of fraud arising from revenue recognition can be rebutted, because: • there is little incentive to manipulate revenue recognition • opportunities to manipulate revenue recognition are very limited • the culture and ethical frameworks of local authorities, including South Somerset District Council, mean that all forms of fraud are seen as unacceptable. Therefore we do not consider this to be a significant risk for South Somerset District Council other than for the fees & charges income stream set out below. In relation to fees and charges, we will: • evaluate the council's accounting policy for recognition of income from fees and charges and evaluate the design of associated controls; and • test, on a sample basis, amounts recognised as income from fees and charges in the financial statements to supporting documentation.
Management over-ride of controls	Council & Group	Under ISA (UK) 240 there is a non-rebuttable presumed risk that the risk of management over-ride of controls is present in all entities. We therefore identified management override of control, in particular journals, management estimates and transactions outside the course of business as a significant risk, which was one of the most significant assessed risks of material misstatement.	We will: • evaluate the design effectiveness of management controls over journals; • analyse the journals listing and determine the criteria for selecting high risk unusual journals; • test unusual journals recorded during the year and after the draft accounts stage for appropriateness and corroboration; • gain an understanding of the accounting estimates and critical judgements applied made by management and consider their reasonableness with regard to corroborative evidence; and • evaluate the rationale for any changes in accounting policies, estimates or significant unusual transactions.

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Significant risks identified

Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
Valuation of land and buildings (Rolling Revaluation)	Council & Group	The Authority revalue land and buildings on a rolling five-yearly basis. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£47m council and £59m group) and the sensitivity of this estimate to changes in key assumptions. Additionally, management will need to ensure the carrying value in the Authority financial statements is not materially different from the current value or the fair value (for surplus assets) at the financial statements date, where a rolling programme is used. We therefore identified valuation of land and buildings, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement.	We will: • evaluate management's processes and assumptions for the calculation of the estimate, the instructions issued to the valuation experts and the scope of their work • evaluate the competence, capabilities and objectivity of the valuation expert • write to the valuer to confirm the basis on which the valuations were carried out • challenge the information and assumptions used by the valuer to assess completeness and consistency with our understanding. • test, on a sample basis, revaluations made during the year to ensure they have been input correctly into the Authority's asset register • evaluate the assumptions made by management for any assets not revalued during the year and how management has satisfied themselves that these are not materially different to current value. • Undertake procedures to confirm that the group Property Plant & Equipment has been included in the group financial statements at the appropriate valuation.
Valuation of Investment Properties	Council	The Authority revalue Investment Properties annually. This valuation represents a significant estimate by management in the financial statements due to the size of the numbers involved (£72.0m) and the sensitivity of this estimate to changes in key assumptions. We therefore identified valuation of Investment Properties, particularly revaluations and impairments, as a significant risk, which was one of the most significant assessed risks of material misstatement.	We will: • evaluate management's processes and assumptions for the calculation of the estimate, the instructions issued to the valuation experts and the scope of their work • evaluate the competence, capabilities and objectivity of the valuation expert • write to the valuer to confirm the basis on which the valuations were carried out • challenge the information and assumptions used by the valuer to assess completeness and consistency with our understanding. • test, on a sample basis, revaluations made during the year to ensure they have been input correctly into the Authority's asset register

Significant risks identified

Risk	Risk relates to	Reason for risk identification	Key aspects of our proposed response to the risk
Valuation of the pension fund net liability	Council	The Authority's pension fund net liability, as reflected in its balance sheet as the net defined benefit liability, represents a significant estimate in the financial statements. The pension fund net liability is considered a significant estimate due to the size of the numbers involved (£79.9m in the Authority's balance sheet) and the sensitivity of the estimate to changes in key assumptions. We therefore identified valuation of the Authority's pension fund net liability as a significant risk, which was one of the most significant assessed risks of material misstatement.	We will: • update our understanding of the processes and controls put in place by management to ensure that the Authority's pension fund net liability is not materially misstated and evaluate the design of the associated controls; • evaluate the instructions issued by management to their management expert (an actuary) for this estimate and the scope of the actuary's work; • assess the competence, capabilities and objectivity of the actuary who carried out the Authority's pension fund valuation; • assess the accuracy and completeness of the information provided by the Authority to the actuary to estimate the liability; • test the consistency of the pension fund asset and liability and disclosures in the notes to the core financial statements with the actuarial report from the actuary; • undertake procedures to confirm the reasonableness of the actuarial assumptions made by reviewing the report of the consulting actuary (as auditor's expert) and performing any additional procedures suggested within the report; and • agree the advance payment made to the pension fund during the year to the expected accounting treatment and relevant financial disclosures. • obtain assurances from the auditor of Somerset Pension Fund as to the controls surrounding the validity and accuracy of membership data; contributions data and benefits data sent to the actuary by the pension fund and the fund assets valuation in the pension fund financial statements.

Accounting estimates and related disclosures

The Financial Reporting Council issued an updated ISA (UK) 540 (revised): *Auditing Accounting Estimates and Related Disclosures* which includes significant enhancements in respect of the audit risk assessment process for accounting estimates.

Introduction

Under ISA (UK) 540 (Revised December 2018) auditors are required to understand and assess an entity's internal controls over accounting estimates, including:

- The nature and extent of oversight and governance over management's financial reporting process relevant to accounting estimates;
- How management identifies the need for and applies specialised skills or knowledge related to accounting estimates;
- How the entity's risk management process identifies and addresses risks relating to accounting estimates;
- The entity's information system as it relates to accounting estimates;
- The entity's control activities in relation to accounting estimates; and
- How management reviews the outcomes of previous accounting estimates.

As part of this process auditors also need to obtain an understanding of the role of those charged with governance, which is particularly important where the estimates have high estimation uncertainty, or require significant judgement.

Specifically do Audit Committee members:

- Understand the characteristics of the methods and models used to make the accounting estimates and the risks related to them;
- Oversee management's process for making accounting estimates, including the use of models, and the monitoring activities undertaken by management; and
- Evaluate how management made the accounting estimates?

Accounting estimates and related disclosures

Additional information that will be required

To ensure our compliance with this revised auditing standard, we will be requesting further information from management and those charged with governance during our audit for the year ended 31 March 2021.

Based on our knowledge of the Council we have identified the following material accounting estimates for which this is likely to apply:

- Valuations of land and buildings (including surplus assets) and investment properties
- Depreciation
- Year end provisions and accruals, specifically provisions for Non Domestic Rate Appeals
- Credit loss and impairment allowances
- Valuation of defined benefit net pension fund liability

The Council's Information systems

In respect of the Council's information systems we are required to consider how management identifies the methods, assumptions and source data used for each material accounting estimate and the need for any changes to these. This includes how management selects, or designs, the methods, assumptions and data to be used and applies the methods used in the valuations.

When the models used include increased complexity or subjectivity, as is the case for many valuation models, auditors need to understand and assess the controls in place over the models and the data included therein. Where adequate controls are not in place we may need to report this as a significant control deficiency and this could affect the amount of detailed substantive testing required during the audit.

If management has changed the method for making an accounting estimate we will need to fully understand management's rationale for this change. Any unexpected changes are likely to raise the audit risk profile of this accounting estimate and may result in the need for additional audit procedures.

We are aware that the Council uses management experts in deriving some of its more complex estimates, e.g. asset valuations and pensions liabilities. However, it is important to note that the use of management experts does not diminish the responsibilities of management and those charged with governance to ensure that:

- All accounting estimates and related disclosures included in the financial statements have been prepared in accordance with the requirements of the financial reporting framework, and are materially accurate;
- There are adequate controls in place at the Council (and where applicable its service provider or management expert) over the models, assumptions and source data used in the preparation of accounting estimates.

Estimation uncertainty

Under ISA (UK) 540 we are required to consider the following:

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- How management understands the degree of estimation uncertainty related to each accounting estimate; and
- How management address this estimation uncertainty when selecting their point estimate.

For example, how management identified and considered alternative, methods, assumptions or source data that would be equally valid under the financial reporting framework, and why these alternatives were rejected in favour of the point estimate used.

The revised standard includes increased emphasis on the importance of the financial statement disclosures. Under ISA (UK) 540 (Revised December 2018), auditors are required to assess whether both the accounting estimates themselves and the related disclosures are reasonable.

Where there is a material uncertainty, that is where there is a significant risk of a material change to the estimated carrying value of an asset or liability within the next year, there needs to be additional disclosures. Note that not all material estimates will have a material uncertainty and it is also possible that an estimate that is not material could have a risk of material uncertainty.

Where there is material estimation uncertainty, we would expect the financial statement disclosures to detail:

- What the assumptions and uncertainties are;
- How sensitive the assets and liabilities are to those assumptions, and why;
- The expected resolution of the uncertainty and the range of reasonably possible outcomes for the next financial year; and
- An explanation of any changes made to past assumptions if the uncertainly is unresolved.

Planning enquiries

As part of our planning risk assessment procedures we sent letter of inquiry that was presented at the council's March Audit Committee, where members endorsed management's responses to our standard planning inquiries.

Further information

Further details on the requirements of ISA (UK) 540 (Revised December 2018) can be found in the auditing standard on the Financial Reporting Council's website:

https://www.frc.org.uk/getattachment/0fa69c03-49ec-49ae-a8c9-cc7a2b65382a/ISA-(UK)-540_Revised-December-2018_final.pdf

Other matters

Other work

In addition to our responsibilities under the Code of Practice, we have a number of other audit responsibilities, as follows:

- We read your Narrative Report and Annual Governance Statement to check that they are consistent with the financial statements on which we give an opinion and our knowledge of the Council.
- We carry out work to satisfy ourselves that disclosures made in your Annual Governance Statement are in line with requirements set by CIPFA.
- We carry out work on your consolidation schedules for the Whole of Government Accounts process in accordance with NAO group audit instructions.
- We consider our other duties under legislation and the Code, as and when required, including:
  - giving electors the opportunity to raise questions about your 2020/21 financial statements, consider and decide upon any objections received in relation to the 2020/21 financial statements;
  - issuing a report in the public interest or written recommendations to the Council under section 24 of the Local Audit and Accountability Act 2014 (the Act).
  - application to the court for a declaration that an item of account is contrary to law under section 28 or a judicial review under section 31 of the Act
  - issuing an advisory notice under section 29 of the Act
- We certify completion of our audit.

Other material balances and transactions

Under International Standards on Auditing, "irrespective of the assessed risks of material misstatement, the auditor shall design and perform substantive procedures for each material class of transactions, account balance and disclosure". All other material balances and transaction streams will therefore be audited. However, the procedures will not be as extensive as the procedures adopted for the risks identified in this report.

Going concern

As auditors, we are required to obtain sufficient appropriate audit evidence regarding, and conclude on:

- whether a material uncertainty related to going concern exists; and
- the appropriateness of management's use of the going concern basis of accounting in the preparation of the financial statements.

The Public Audit Forum has been designated by the Financial Reporting Council as a "SORP-making body" for the purposes of maintaining and updating Practice Note 10: Audit of financial statements and regularity of public sector bodies in the United Kingdom (PN 10). It is intended that auditors of public sector bodies read PN 10 in conjunction with (ISAs) (UK).

PN 10 has recently been updated to take account of revisions to ISAs (UK), including ISA (UK) 570 on going concern. The revisions to PN 10 in respect of going concern are important and mark a significant departure from how this concept has been audited in the public sector in the past. In particular, PN 10 allows auditors to apply a 'continued provision of service approach' to auditing going concern, where appropriate. Applying such an approach should enable us to increase our focus on wider financial resilience (as part of our VfM work) and ensure that our work on going concern is proportionate for public sector bodies. We will review the Council's arrangements for securing financial sustainability as part of our Value for Money work and provide a commentary on this in our Auditor's Annual Report (see page 17).

Materiality

The concept of materiality

Materiality is fundamental to the preparation of the financial statements and the audit process and applies not only to the monetary misstatements but also to disclosure requirements and adherence to acceptable accounting practice and applicable law. Misstatements, including omissions, are considered to be material if they, individually or in the aggregate, could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

Materiality for planning purposes

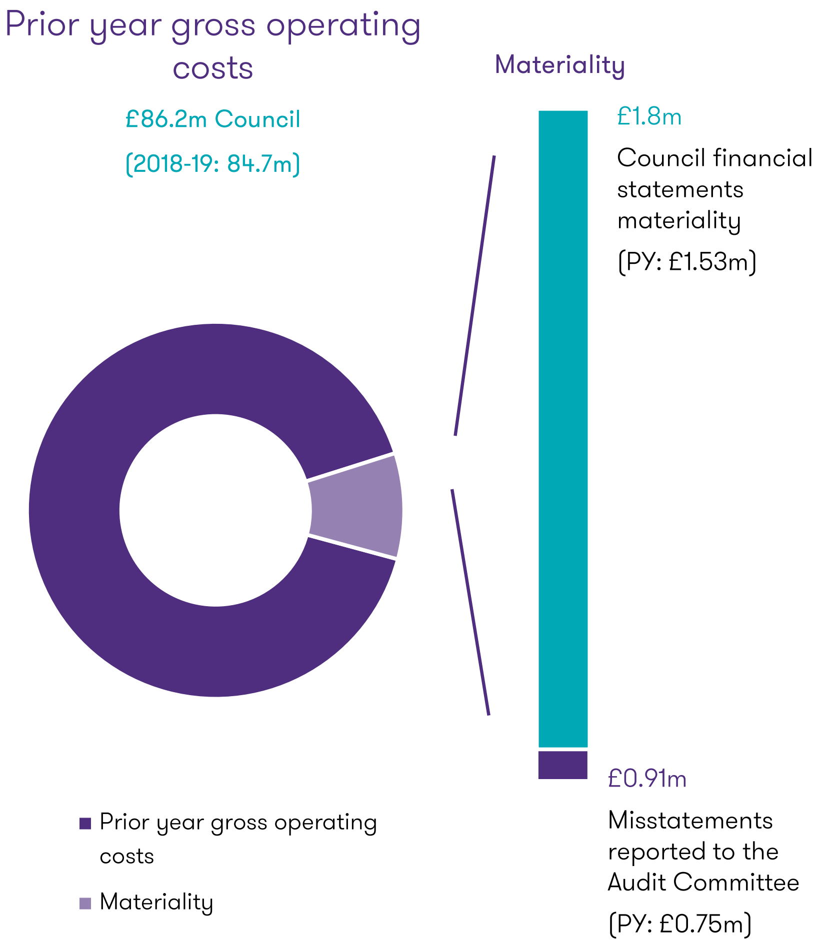
We have determined financial statement materiality based on a proportion of the gross expenditure of the Council for the financial year. In the prior year we used the same benchmark. Materiality at the planning stage of our audit is £1.9mm (PY £1.64m) for the group, which equates to 1.4% of Group assets and £1.8m (PY 1.53m) for the Council, which equates to 2% of your forecast gross expenditure for the year. We design our procedures to detect errors in specific accounts at a lower level of precision which we have determined to be £20k for Senior officer renumeration.

We reconsider planning materiality if, during the course of our audit engagement, we become aware of facts and circumstances that would have caused us to make a different determination of planning materiality.

Matters we will report to the Audit Committee

Whilst our audit procedures are designed to identify misstatements which are material to our opinion on the financial statements as a whole, we nevertheless report to the Audit Committee any unadjusted misstatements of lesser amounts to the extent that these are identified by our audit work. Under ISA 260 (UK) 'Communication with those charged with governance', we are obliged to report uncorrected omissions or misstatements other than those which are 'clearly trivial' to those charged with governance. ISA 260 (UK) defines 'clearly trivial' as matters that are clearly inconsequential, whether taken individually or in aggregate and whether judged by any quantitative or qualitative criteria. In the context of the Council, we propose that an individual difference could normally be considered to be clearly trivial if it is less than £0.91m (PY £0.75m).

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



Value for Money arrangements

Revised approach to Value for Money work for 2020/21

On 1 April 2020, the National Audit Office introduced a new Code of Audit Practice which comes into effect from audit year 2020/21. The Code introduced a revised approach to the audit of Value for Money. (VFM)

There are three main changes arising from the NAO's new approach:

- A new set of key criteria, covering financial sustainability, governance and improvements in economy, efficiency and effectiveness
- More extensive reporting, with a requirement on the auditor to produce a commentary on arrangements across all of the key criteria, rather than the current 'reporting by exception' approach
- The replacement of the binary (qualified / unqualified) approach to VFM conclusions, with far more sophisticated judgements on performance, as well as key recommendations on any significant weaknesses in arrangements identified during the audit.

The Code require auditors to consider whether the body has put in place proper arrangements to secure economy, efficiency and effectiveness in its use of resources. When reporting on these arrangements, the Code requires auditors to structure their commentary on arrangements under three specified reporting criteria. These are as set out below:

Improving economy, efficiency and effectiveness

Arrangements for improving the way the body delivers its services. This includes arrangements for understanding costs and delivering efficiencies and improving outcomes for service users.

Financial Sustainability

Arrangements for ensuring the body can continue to deliver services. This includes planning resources to ensure adequate finances and maintain sustainable levels of spending over the medium term (3-5 years)

Governance

Arrangements for ensuring that the body makes appropriate decisions in the right way. This includes arrangements for budget setting and management, risk management, and ensuring the body makes decisions based on appropriate information

Risks of significant VFM weaknesses

As part of our planning work, we considered whether there were any risks of significant weakness in the body's arrangements for securing economy, efficiency and effectiveness in its use of resources that we needed to perform further procedures on. At this stage we have not identified any risks, however we have identified a number of areas of focus, which are detailed below, along with the further procedures we will perform. We may need to make recommendations following the completion of our work. The potential different types of recommendations we could make are set out on the following page.

Areas of focus

Those areas requiring audit consideration and procedures to address the likelihood that proper arrangements are not in place at the body to deliver value for money.

The council's external commercialisation strategy and it's impact on the Medium term Financial Strategy.

The councils commercialisation strategy forms a significant part of the MTFS.

We will review the council's investment strategies, and decision making processes to determine whether there are adequate arrangements to secure value for money. We will also review the impact of the pandemic on the council's strategy.

The council's priorities post transformation.

Having recently completed an ambitious transformation programme, there is a risk that the council's monitoring and reporting of transformation related priorities does not continue and is not effectively aligned with the councils other plans (e.g. finance plans, workforce plans or capital plans).

We will review the council's post-transformation reporting, to determine whether the anticipated benefits continue to be fully realised and monitored and there are appropriate links with other council priorities.

Arrangements for securing value for money in the council's local government reorganisation proposals

The council is collaborating with other Somerset Districts to propose a two unitary authority approach to Somerset as part of the consultation on local government reorganisation in Somerset.

We will review the council's processes for collaborating with other districts and will review South Somerset's governance arrangements including the information and advice sought and provided to members to inform decision making.

The council's arrangements to maintain a strong leadership team with the right skills and experience

The council has seen a relatively high level of senior staff turnover in the last couple of years. There is a risk that this high level of turnover in the skills and experience of the leadership team could impact on the Council maintaining its strategic direction and delivery of its corporate priorities.

We will review the succession arrangements that the Council has in place to ensure the smooth transition and induction of new senior staff.

Amended governance arrangements in light of the coronavirus pandemic

To ensure emergency decisions could be taken at short notice, the council gave delegated authority to the leader and chief executive during 2020-21. There is a risk that the use of these delegated powers were not appropriately monitored and reviewed in a timely way.

We will review the delegated powers to understand their limits and the processes in place to monitor and review the appropriateness of their continued use.

Risks of significant VFM weaknesses

As part of our planning work, we considered whether there were any risks of significant weakness in the body's arrangements for securing economy, efficiency and effectiveness in its use of resources that we needed to perform further procedures on. The area of focus we have identified are detailed in the first table on the previous page, along with the further procedures we will perform. We may need to make recommendations following the completion of our work. The potential different types of recommendations we could make are set out in the second table below.

Potential types of recommendations

A range of different recommendations could be made following the completion of work on risks of significant weakness, as follows:

Statutory recommendation

Written recommendations to the body under Section 24 (Schedule 7) of the Local Audit and Accountability Act 2014. A recommendation under schedule 7 requires the body to discuss and respond publicly to the report.

Key recommendation

The Code of Audit Practice requires that where auditors identify significant weaknesses in arrangements to secure value for money they should make recommendations setting out the actions that should be taken by the body. We have defined these recommendations as 'key recommendations'.

Improvement recommendation

These recommendations, if implemented should improve the arrangements in place at the body, but are not made as a result of identifying significant weaknesses in the body's arrangements

Audit logistics and team

Audit committee March

Audit committee May

Audit committee September

Audit committee September

Planning and risk assessment

Informing the Audit Risk Assessment

Interim audit March - April

Audit Plan

Year end audit July - September

Audit Findings Report/Draft Auditor's Annual Report

Audit opinion

Auditor's Annual Report

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Barrie Morris, Key Audit Partner

Barrie leads our relationship with you and is a key contact for the Chief Executive, Section 151 Officer and the Audit Committee. Barrie takes overall responsibility for the delivery of a high quality audit, meeting the highest professional standards and adding value to the Council.

Beth Garner, Audit Manager

Beth's role involves overseeing the day to day planning and execution of the audit, ensuring the audit requirements are fully complied with and producing reports for the Audit Committee. She will respond to ad-hoc queries whenever raised and meet regularly with the Section 151 Officer and members of the finance team

Audited body responsibilities

Where audited bodies do not deliver to the timetable agreed, we need to ensure that this does not impact on audit quality or absorb a disproportionate amount of time, thereby disadvantaging other audits. Where the elapsed time to complete an audit exceeds that agreed due to a client not meeting its obligations we will not be able to maintain a team on site. Similarly, where additional resources are needed to complete the audit due to a client not meeting their obligations we are not able to guarantee the delivery of the audit to the agreed timescales. In addition, delayed audits will incur additional audit fees.

Our requirements

To minimise the risk of a delayed audit, you need to ensure that you:

- produce draft financial statements of good quality by the agreed timetable you have agreed with us, including all notes, the Narrative Report and the Annual Governance Statement
- ensure that good quality working papers are available at the start of the audit, in accordance with the working paper requirements schedule that we have shared with you
- ensure that the agreed data reports are available to us at the start of the audit and are reconciled to the values in the accounts, in order to facilitate our selection of samples for testing
- ensure that all appropriate staff are available on site throughout (or as otherwise agreed) the planned period of the audit
- respond promptly and adequately to audit queries.

Audit fees

In 2017, PSAA awarded a contract of audit for South Somerset District Council to begin with effect from 2018/19. The fee agreed in the contract was £37,943. Since that time, there have been a number of developments, particularly in relation to the revised Code and ISA's which are relevant for the 2020/21 audit.

As referred to on page 17, the 2020/21 Code introduces a revised approach to our VFM work. This requires auditors to produce a commentary on arrangements across all of the key criteria, rather than the current 'reporting by exception' approach. Auditors now have to make far more sophisticated judgements on performance, as well as issue key recommendations if any significant weaknesses in arrangements are identified during the audit. We will be working with the NAO and other audit firms to discuss and share learning in respect of common issues arising across the sector.

The new approach will be more challenging for audited bodies, involving discussions at a wider and more strategic level. Both the reporting, and the planning and risk assessment which underpins it, will require more audit time, delivered through a richer skill mix than in previous years. Our estimate is that for your audit, this will result in an increased fee of £9,000 (24%). This is in line with increases we are proposing at all our local audits.

Additionally, across all sectors and firms, the FRC has set out its expectation of improved financial reporting from organisations and the need for auditors to demonstrate increased scepticism and challenge and to undertake additional and more robust testing, as noted in the number of revised ISA's issued by the FRC that are applicable to audits of financial statements commencing on or after 15 December 2019, as detailed in Appendix 1.

As a firm, we are absolutely committed to meeting the expectations of the FRC with regard to audit quality and public sector financial reporting. Our proposed work and fee for 2020/21, as set out below, is detailed overleaf and has been discussed with the Section 151 Officer and is subject to PSAA agreement.

	Actual Fee 2018/19	**Actual Fee 2019/20**	**Proposed fee 2020/21**
South Somerset District Council Audit	£42,443	£69,759	£66,943
Total audit fees (excluding VAT)	£42,443	£69,759	£66,943

Assumptions

In setting the above fees, we have assumed that the Council will:

- prepare a good quality set of accounts, supported by comprehensive and well presented working papers which are ready at the start of the audit
- provide appropriate analysis, support and evidence to support all critical judgements and significant judgements made during the course of preparing the financial statements
- provide early notice of proposed complex or unusual transactions which could have a material impact on the financial statements.

Relevant professional standards

In preparing our fee estimate, we have had regard to all relevant professional standards, including paragraphs 4.1 and 4.2 of the FRC's Ethical Standard (revised 2019) which stipulate that the Engagement Lead (Key Audit Partner) must set a fee sufficient to enable the resourcing of the audit with partners and staff with appropriate time and skill to deliver an audit to the required professional and Ethical standards.

Audit fees – detailed analysis

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Scale fee published by PSAA	£37,943
Ongoing increases to scale fee first identified in 2019/20	
Raising the bar/regulatory factors	£2,500
Enhanced audit procedures for Property, Plant and Equipment	£1,750
Enhanced audit procedures for Pension Liabilities (IAS19)	£1,750
Brought forward ongoing fee from 2019/20	£43,943
New issues for 2020/21	
Additional work on Value for Money (VfM) under new NAO Code	£9,000
Estimated cost of our Auditor's expert	£3,500
Increased audit requirements of revised ISAs 540 / 240 / 700	£6,500
Audit of Group Accounts (not included in the Scale Fee)	£4,000
Total proposed audit fees 2020/21 (excluding VAT)	£66,943

All variations to the scale fee will need to be approved by PSAA

Independence and non-audit services

Auditor independence

Ethical Standards and ISA (UK) 260 require us to give you timely disclosure of all significant facts and matters that may bear upon the integrity, objectivity and independence of the firm or covered persons. relating to our independence. We encourage you to contact us to discuss these or any other independence issues with us. We will also discuss with you if we make additional significant judgements surrounding independence matters.

We confirm that there are no significant facts or matters that impact on our independence as auditors that we are required or wish to draw to your attention. We have complied with the Financial Reporting Council's Ethical Standard (Revised 2019) and we as a firm, and each covered person, confirm that we are independent and are able to express an objective opinion on the financial statements. Further, we have complied with the requirements of the National Audit Office's Auditor Guidance Note 01 issued in May 2020 which sets out supplementary guidance on ethical requirements for auditors of local public bodies.

We confirm that we have implemented policies and procedures to meet the requirements of the Ethical Standard. For the purposes of our audit we have made enquiries of all Grant Thornton UK LLP teams providing services to the Council.

Other services

No other services provided by Grant Thornton were identified.

Service	Fees £	Threats	Safeguards
Audit related			
Certification of Housing Benefits claim	23,000	Self-Interest (because this is a recurring fee)	The level of this recurring fee taken on its own is not considered a significant threat to independence as the fee for this work, relative to Grant Thornton UK LLP's turnover overall. Further, it is a fixed fee and there is no contingent element to it. These factors mitigate the perceived self-interest threat to an acceptable level.

Appendix 1: Revised Auditor Standards and application guidance

FRC revisions to Auditor Standards and associated application guidance

The following Auditing Standards and associated application guidance that were applicable to 19/20 audits, have been revised or updated by the FRC, with additional requirements for auditors for implementation in 2020/21 audits and beyond.

	Date of revision	Application to 2020/21 Audits
ISQC (UK) 1 – Quality Control for Firms that Perform Audits and Reviews of Financial Statements, and other Assurance and Related Service Engagements	November 2019	✓
ISA (UK) 200 – Overall Objectives of the Independent Auditor and the Conduct of an Audit in Accordance with International Standards on Auditing (UK)	January 2020	✓
ISA (UK) 220 – Quality Control for an Audit of Financial Statements	November 2019	✓
ISA (UK) 230 – Audit Documentation	January 2020	✓
ISA (UK) 240 – The Auditor's Responsibilities Relating to Fraud in an Audit of Financial Statements	January 2020	✓
ISA (UK) 250 Section A – Consideration of Laws and Regulations in an Audit of Financial Statements	November 2019	✓
ISA (UK) 250 Section B – The Auditor's Statutory Right and Duty to Report to Regulators od Public Interest Entities and Regulators of Other Entities in the Financial Sector	November 2019	✓

Appendix 1: Revised Auditor Standards and application guidance continued

	Date of revision	Application to 2020/21 Audits
ISA (UK) 260 – Communication With Those Charged With Governance	January 2020	✓
ISA (UK) 315 – Identifying and Assessing the Risks of Material Misstatement Through Understanding of the Entity and Its Environment	July 2020	
ISA (UK) 500 – Audit Evidence	January 2020	✓
ISA (UK) 540 – Auditing Accounting Estimates and Related Disclosures	December 2018	✓
ISA (UK) 570 – Going Concern	September 2019	✓
ISA (UK) 580 – Written Representations	January 2020	✓
ISA (UK) 600 - Special considerations – Audits of Group Financial Statements (Including the Work of Component Auditors)	November 2019	✓
ISA (UK) 620 – Using the Work of an Auditor's Expert	November 2019	✓
ISA (UK) 700 – Forming an Opinion and Reporting on Financial Statements	January 2020	✓

Appendix 1: Revised Auditor Standards and application guidance continued

	Date of revision	Application to 2020/21 Audits
ISA (UK) 701 – Communicating Key Audit Matters in the Independent Auditor's Report	January 2020	✓
ISA (UK) 720 – The Auditor's Responsibilities Relating to Other Information	November 2019	✓
Practice Note 10: Audit of Financial Statements of Public Sector Bodies in the United Kingdom	December 2020	✓

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South Somerset District Council

SWAP Internal Audit Outturn Report 2020-21

SWAP Internal Audit Outturn Report 2020-21

SWAP CEO:	Dave Hill – Chief Executive - SWAP
Lead Officer:	Alastair Woodland – Assistant Director
Contact Details:	Alastair.Woodland@SWAPAudit.co.uk

Purpose of the Report

To update members on the Internal Audit Plan 2020/21 Outturn and bring to their attention any significant findings identified through our work.

Public Interest

Audit committees are a key component of an authority's governance framework. Their function is to provide an independent and high-level resource to support good governance and strong public financial management.

The purpose of an audit committee is to provide to those charged with governance independent assurance on the adequacy of the risk management framework, the internal control environment and the integrity of the financial reporting and governance processes.

Recommendations

1. Members are asked to note progress made in delivery of the 2020/21 internal audit plan and the significant findings since the previous update.

Background

The Internal Audit function plays a central role in corporate governance by providing independent assurance to the Audit Committee over the effectiveness of internal controls, governance and risk management. The 2020/21 Annual Audit Plan was approved by the Audit Committee at its May 2020 meeting and is to provide independent and objective assurance on SSDC's Internal Control Environment and this work will support the Annual Governance Statement.

Report Detail

This report summarises the work of the Council's Internal Audit Service and provides:

- Details of any new significant weaknesses identified during internal audit work completed since the last report to the committee in March 2021.

- A schedule of audits completed during the period, detailing their respective assurance opinion rating, the number of recommendations and the respective priority rankings of these.

Please refer to the attached SWAP Outturn Report 2020-21 for further details.

Financial Implications

There are no financial implications associated with these recommendations.

Council Plan Implications

Delivery of corporate objectives requires strong internal control. The attached report provides a summary of the audit work carried out to date this year by the Council's internal auditors, SWAP Internal Audit Services.

Carbon Emissions and Climate Change Implications

There are no implications arising from this report.
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Equality and Diversity Implications

There are no implications arising from this report.

Background Papers

- Internal Audit Plan and Charter 2020-21 May 2020
- Internal Audit Progress Update Report July 2020
- Internal Audit Progress Update Report October 2020
- Internal Audit Progress Update Report January 2021
- Internal Audit Progress Update Report March 2021

South Somerset District Council

Report of Internal Audit Activity

2020-21 Outturn Report May 2021

Internal Audit ▪ Risk ▪ Special Investigations ▪ Consultancy

Contents

The contacts at SWAP in connection with this report are:

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Alastair Woodland
Assistant Director
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alastair.woodland@swapaudit.co.uk

Internal Audit Plan Progress 2020-21

Our audit activity is split between:

- **Operational Audit**
- **Governance Audit**
- **Key Control Audit**
- **IT Audit**
- **Grants**
- **Other Reviews**

Role of Internal Audit

The Internal Audit service for the South Somerset District Council is provided by South West Audit Partnership Limited (SWAP). SWAP is a Local Authority controlled Company. SWAP has adopted and works to the Standards of the Institute of Internal Auditors, further guided by interpretation provided by the Public Sector Internal Audit Standards (PSIAS), and also follows the CIPFA Code of Practice for Internal Audit. The Partnership is also guided by the Internal Audit Charter approved by the Audit and Governance Committee at its meeting in May 2020.

Internal Audit provides an independent and objective opinion on the Authority's control environment by evaluating its effectiveness. Primarily the work includes:

- Operational Audit Reviews
- Cross Cutting Governance Audits
- Annual Review of Key Financial System Controls
- IT Audits
- Grants
- Other Special or Unplanned Review

Internal Audit work is largely driven by an Annual Audit Plan. This is approved by the Section 151 Officer, following consultation with the Senior Management Team. This year's Audit Plan was reported to and approved by this Committee at its meeting in May 2020. Audit assignments are undertaken in accordance with this Plan to assess current levels of governance, control and risk.

Internal Audit Plan Progress 2020-21

Outturn to Date:

We rank our recommendations on a scale of 1 to 3, with 3 being minor or administrative concerns to 1 being areas of major concern requiring immediate corrective action.

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Internal Audit Work programme Update

The schedule provided at **Appendix B** contains a list of all audits as agreed in the Annual Audit Plan 2020/21. It is important that Members are aware of the status of all audits and that this information helps them place reliance on the work of Internal Audit and its ability to complete the plan as agreed.

Each completed assignment includes its respective "assurance opinion" rating together with the number and relative ranking of recommendations that have been raised with management. In such cases, the Committee can take assurance that improvement actions have been agreed with management to address these. The assurance opinion ratings have been determined in accordance with the Internal Audit "Audit Framework Definitions" as detailed on **Appendix A** of this document.

The following table summarised Audits finalised since the last update in March 2020:

Audit Area	Quarter	Status	Opinion
Creditors	3	Final	Reasonable
Income Generation Service Improvements	3	Final	Limited
Budget Planning and Monitoring	3	Final	Reasonable
NEW: Council Baseline Assessment of maturity for Fraud	4	Final	Non-Opinion
ICT Governance and Risk Scope Review	4	Final	Non-Opinion
NEW: Business Grants - Post Assurance Review	4	Final	Substantial
Ethical Governance	4	Final	Reasonable

Significant Corporate Risks

Identified Significant Corporate Risks should be brought to the attention of the Audit Committee.

Completed Assignments:

Summary of work completed with a focus on the high priority issues that we believe should be brought to the attention of the Audit Committee.

- **Limited or No Assurance Opinions**
- **Follow-ups**

Significant Corporate Risks

We provide a definition of the 3 Risk Levels applied within audit reports and these are detailed in **Appendix A**. For those audits which have reached report stage through the year, I will report risks we have assessed as 'High'.

In this update there are no final reports included with significant corporate risks.

Summary of Work Completed – Limited or No Assurance Opinions

Income Generation – Limited Assurance

The Council approved a Commercial Strategy which included a target for increasing the yield across all Council services by 5% annually. The audit was carried out to assess how the Council was progressing against this target. In 2018/19 the Council achieved 4.5% overall. For the 2019/20 financial year the calculations to identify how the Council did against their target was not completed before the audit was completed in Q4, delays in completing this are due to Covid-19. Without this information we are unable to provide anything more than Limited assurance as we are unable to assess the impact of the work that has been undertaken.

The audit identified that while good templates had been developed for assessing fees and charges and for completing new business cases needed to help ensure the Council can reach the targets these had not been rolled out. The progress of this has be greatly hindered due to Covid-19 diverting resource aware for this work towards Covid recovery and the increased work for the service areas reducing their availability to work through this.

No	Weaknesses Found	Risk Identified	Recommendation Action	Managers Agreed Action	Agreed Date of Action
Income Generation – Service Delivery					
1	2019/20 progress against target had not been calculated	Council failed to meet their target reducing the available financial resources	Move towards real time data for performance monitoring which will capture the progress towards the 5% target.	Agreed	1st January 2022
2	Fees and Charges have only been calculated for 2 service areas	Council are undercharging and not covering their own costs or achieving income where allowed reducing the financial resources available	Six to eight services completed for by the time of the fee and charges annual review.	Agreed	31st October 2021

Completed Assignments:

Summary of work completed with a focus on the high priority issues that we believe should be brought to the attention of the Audit Committee.

- **Limited or No Assurance Opinions**
- **Follow-ups**

Summary of Work Completed

Baseline Assessment of Maturity in relation to Fraud

Local authorities have responsibilities for the effective stewardship of public money and for safeguarding against losses due to fraud and corruption. The audit committee should have oversight of the authority's counter fraud strategy, assessing whether it meets recommended practice and governance standards and complies with legislation such as the Bribery Act 2010.

To assist in this oversight a baseline assessment has been completed at South Somerset District Council in line with requirements of the Fighting Fraud and Corruption Locally Strategy. Each of the 27 requirements have been given a red, amber or green, rating based on a corporate view across the organisation. The report for this work comes complete with an action roadmap for improvement and can be revisited in 12 months' time to demonstrate the direction of travel and any progress, including the improvement of maturity position. A full copy of the report and findings has been shared with the Audit Committee, together with the wider benchmarking report. The below chart summarises the assessments outcomes against the 6 key theme area.

Baseline Assessment of Six Themed Areas

The Assistant Director for SWAP reports performance on a regular basis to the SWAP Management and Partnership Boards.

SWAP Performance

SWAP now provides the Internal Audit service for 24 public sector bodies. SWAP performance is subject to regular monitoring review by both the Board and the Member Meetings. The respective outturn performance results for South Somerset District Council for the 2020/21 (as of 10 May 2021) were as follows:

Performance Target	Target Year End	Average Performance
Audit Plan – Percentage Progress Final, Draft and Discussion In progress Yet to complete	>90%	90% 10% 0%
Quality of Audit Work Customer Satisfaction Questionnaire	>95%	100%
Outcomes from Audit Work Value to the Organisation *(client view of whether our audit work met or exceeded expectations, in terms of value to their area)*	>95%	100%

We keep our audit plans under regular review so as to ensure that we are auditing the right things at the right time. Due to Covid-19 the plan priority areas will be agreed on a quarter-by-quarter basis.

Approved Changes to the Plan

The audit plan for 2020/21 is detailed in **Appendix B.** Due to the impact of Covid-19 and the requests for some additional work to be added to the plan during the year we have had to remove some audits from the annual plan. The Plan has remained flexible throughout the year and targeted short-term priorities as agreed with SLT on a quarterly basis. There are no changes to the 2020-21 Audit Plan since our last update report to Audit Committee in March 2021.

Internal Audit Definitions — Appendix A

Assurance Definitions

No	Immediate action is required to address fundamental gaps, weaknesses or non-compliance identified. The system of governance, risk management and control are inadequate to effectively manage risks to the achievement of objectives in the area audited.
Limited	Significant gaps, weaknesses or non-compliance were identified. Improvement is required to the system of governance, risk management and control to effectively manage risks to the achievement of objectives in the area audited.
Reasonable	There is a generally sound system of governance, risk management and control in place. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives in the area audited.
Substantial	A sound system of governance, risk management and control exist, with internal controls operating effectively and being consistently applied to support the achievement of objectives in the area audited.
Non-Opinion/Advisory	In addition to our opinion-based work we will provide consultancy services. The “advice” offered by Internal Audit in its consultancy role may include risk analysis and evaluation, developing potential solutions to problems and providing controls assurance.

Definition of Corporate Risks

Risk	Reporting Implications
High	Issues that we consider need to be brought to the attention of both senior management and the Audit Committee.
Medium	Issues which should be addressed by management in their areas of responsibility.
Low	Issues of a minor nature or best practice where some improvement can be made.

Categorisation of Recommendations

In addition to the corporate risk assessment it is important that management know how important the recommendation is to their service. Each recommendation has been given a priority rating at service level with the following definitions:

Priority 1	Findings that are fundamental to the integrity of the service’s business processes and require the immediate attention of management.
Priority 2	Important findings that need to be resolved by management.
Priority 3	Finding that requires attention.

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
FINAL									
Fraud, Corruption and Governance	Boden Mill & Chard Regeneration Scheme Accounts Review	Q1	Final	Advisory	0	0	0	0	
Fraud, Corruption and Governance	**New:** Growth Deal Capital Expenditure Certification	Q1	Final	Advisory	0	0	0	0	
Fraud, Corruption and Governance	Yeovil Cemetery & Crematorium Annual Accounts Controls Assurance	Q1	Final	Advisory	0	0	0	0	
Covid-19 Support	**New:** Covid-19 Support/Advice	Q1	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	Project Governance - Regeneration Projects	Q1	Final	Limited	5	0	3	2	
Follow Up	Combined Follow up	Q1	Final	Follow up	0	0	0	0	
Covid-19 Support	**NEW:** Grant Funding Schemes Assurance for Local Authorities (Risk Assessment)	Q1	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	**NEW:** Health & Wellbeing	Q2	Final	Reasonable	2	0	0	2	
Operational	Homelessness	Q2	Final	Limited	5	0	3	2	
ICT	Cyber Security Framework Review	Q3	Final	Advisory	20 key Control areas reviewed. Reported separately to Audit Committee.				
Covid-19 Support	**NEW:** Local restriction Grant Support	Q3	Final	Advisory	0	0	0	0	Support work

Summary of Work Plan

Appendix B

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
Governance Fraud & Corruption	Income Generation Service Improvements	Q3	Final	Limited	3	0	2	1	
Key Control	Budget Planning and Monitoring	Q3	Final	Reasonable	2	0	0	2	
ICT	ICT Governance and Risk Scope Review	Q3	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	**NEW:** Covid-19 Grant Processing Support	Q4	Final	Advisory	0	0	0	0	Support work
Covid-19 Support	**NEW:** Grant Support – Bank detail checks	Q4	Final	Advisory	0	0	0	0	Support work
Governance Fraud & Corruption	**NEW:** Council Baseline Assessment of maturity for Fraud	Q4	Final	Advisory	0	0	0	0	Action plan provided – Report provided to Audit Committee Members
Covid-19 Support	**NEW:** Business Grants - Post Assurance Review	Q4	Final	Substantial	0	0	0	0	
Key Control	Creditors	Q4	Final	Reasonable	3	0	1	2	
Governance Fraud & Corruption	Ethical Governance	Q4	Final	Reasonable	5	0	1	4	Survey Report and Framework Report
Governance Fraud & Corruption	**NEW:** Compliance & Enforcement Grant	Q4	Final	Advisory	0	0	0	0	
Draft									
Transformation	Transformation closedown	Q2	Draft						
Follow Up	Information Governance GDPR Follow Up	Q4	Draft						

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
Operational	S106 & CIL	Q4	Draft						
Governance Fraud & Corruption	**NEW:** Fraud Risk – Impact of Covid-19	Q4	Drafting						
In Progress									
Governance Fraud & Corruption	Commercial Investments	Q3	In progress						
Governance Fraud & Corruption	Risk Management	Q4	In Progress						
Governance Fraud & Corruption	**NEW:** Fraud Risk Assessment	Q4	In Progress						
Deferred or Removed									
Transformation	Civica Digital Systems Review	Q2							Combined with Transformation Close down
Governance Fraud & Corruption	Somerset Districts Cooperation/collaboration FOLGIS	Q4							**NEW:** Covid-19 Support/Advice **NEW:** Grant Funding Schemes Assurance for Local Authorities (Risk Assessment)
Governance Fraud & Corruption	Climate Change	Q4							
ICT	Digital Strategy & Transformation	Q3							Pushed back due ICT audits bottleneck. Replaced by Health & Wellbeing
Governance Fraud & Corruption	Yeovil Innovation Centre (YIC) Phase 2	Q4							**NEW:** Local restriction Grant Support Q3 **NEW:** Grant Support – Bank detail checks Q4

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major Recommendation 1	2	3 = Minor 3	Comments
Key Control	Council Tax & NNDR	Q4							**NEW:** Council Baseline Assessment of maturity for Fraud **NEW:** Fraud Risk Assessment **NEW:** Fraud Risk – Impact of Covid-19 **NEW:** Covid-19 Grant Processing Support Q4 **NEW:** Compliance & Enforcement Grant Management provided an update to Audit Committee in March for Housing Benefits and CTax. Procurement – Leisure is earmarked for Q1 2021-22
Key Control	Housing Benefits	Q4							
Governance Fraud & Corruption	Procurement – Leisure Contract	Q4							

South Somerset District Council

Internal Annual Opinion Report 2020-21

Internal Annual Opinion Report 2020-21

SWAP CEO David Hill – Chief Executive SWAP
Lead Officer: Alastair Woodland – Assistant Director
Contact Details: Alastair.woodland@southsomerset.co.uk

Purpose of the Report

This report provides an update on the position of the Internal Audit Plan at the end of 2020/21 and also provides Internal Audit's overall 'Opinion' on the systems of governance, risk management and internal control at South Somerset District Council.

Public Interest

The Head of Internal Audit (SWAP Assistant Director) should provide a written annual report to those charged with governance to support the Authority's Annual Governance Statement (AGS).

Recommendations

1. Members are asked to note the Annual Opinion on the effectiveness of governance, risk management and internal control in the delivery of SSDC objectives.

Background

The Audit Committee agreed the original 2020/21Internal Audit Plan at its May 2020 meeting, with progress updates provided during the year.

This report summarises the work of the Council's Internal Audit Service and provides:

- A summary of the key risks that were identified during the 2020/21 financial year.
- A schedule of audits completed during the period, detailing their respective assurance opinion rating, the number of recommendations and the respective priority rankings of these.

The Audit Opinion for 2020/21 is contained within the attached SWAP report.

Report Detail

Please refer to the attached SWAP Annual Opinion Report 2020-21

Financial Implications

There are no financial implications associated with these recommendations.

Council Plan Implications

Delivery of corporate objectives requires strong internal control. The attached report provides a summary of the audit work carried out to date this year by the Council's internal auditors, SWAP Internal Audit Services.

Carbon Emissions and Climate Change Implications

There are no implications arising from this report.

Equality and Diversity Implications

There are no implications arising from this report.

Background Papers

- Internal Audit Plan and Charter 2020-21 May 2020
- Internal Audit Progress Update Report July 2020
- Internal Audit Progress Update Report October 2020
- Internal Audit Progress Update Report January 2021
- Internal Audit Progress Update Report March 2021
- Internal Audit Outturn Report May 2021

South Somerset District Council

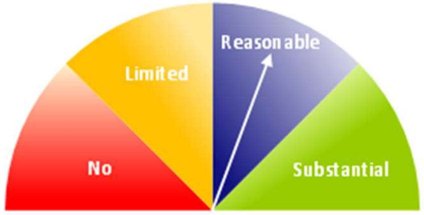
Internal Audit Annual Opinion Report 2020/21

Internal Audit ▪ Risk ▪ Special Investigations ▪ Consultancy

Unrestricted

Internal Audit Annual Opinion – 2020/21: ‘At a Glance’

Annual Opinion



There is generally a sound system of governance, risk management and control in place. Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives.

The Headlines

No Significant Risk identified in year after testing the controls in place.
28 reviews delivered as part of the 2020/21 Internal Audit Plan. Includes assurance, advisory and follow up reviews (21 final, 4 Draft, 3 in progress).
Internal Audit staff redeployed directly into Council areas to assist with the COVID response. COVID 19 Business Grant processing and post payment checks.
Range of innovations and enhancements made to our internal audit process throughout the year. One-page audit report, introduction of Agile auditing and planning.

Internal Audit Assurance Opinions 2020/21 *	
Substantial	**1**
Reasonable	4
Limited	3
No Assurance	0
Advisory / Follow Up	13

Internal Audit Agreed Actions 2020/21*	
Priority 1	0
Priority 2	10
Priority 3	15
Total	25

*Final Reports only

SWAP work is completed to comply with the International Professional Practices Framework of the Institute of Internal Auditors, further guided by interpretation provided by the Public Sector Internal Audit Standards (PSIAS) and the CIPFA Local Government Application Note.

Executive Summary

Internal Audit provides an independent and objective opinion on the effectiveness of the Authority's risk management, control and governance processes.

Purpose

The Head of Internal Audit (SWAP Assistant Director) should provide a written annual report to those charged with governance to support the Authority's Annual Governance Statement (AGS). This report should include the following:

- An opinion on the overall adequacy and effectiveness of the organisation's governance, risk management and internal control environment, including an evaluation of the following:
  - the design, implementation and effectiveness of the organisation's ethics-related objectives, programmes and activities;
  - whether the information technology governance of the organisation supports the organisation's strategies and objectives;
  - the effectiveness of risk management processes; and
  - the potential for the occurrence of fraud and how the organisation manages fraud risk.
- Disclose any qualifications to that opinion, together with the reasons for the qualification.
- Present a summary of the audit work from which the opinion is derived, including reliance placed on work by other assurance bodies.
- Draw attention to any issues the Head of Internal Audit judges particularly relevant to the preparation of the Annual Governance Statement.
- Compare the work actually undertaken with the work that was planned and summarise the performance of the internal audit function against its performance measures and criteria.
- Comment on compliance with these standards and communicate the results of the internal audit quality assurance programme.

The purpose of this report is to satisfy this requirement and Members are asked to note its content and the Annual Internal Audit Opinion given.

Executive Summary

Three Lines Model

To ensure the effectiveness of an organisation's risk management framework, the Audit and Governance Committee and senior management need to be able to rely on adequate line functions – including monitoring and assurance functions – within the organisation.

The 'Three Lines' model is a way of explaining the relationship between these functions and as a guide to how responsibilities should be divided:

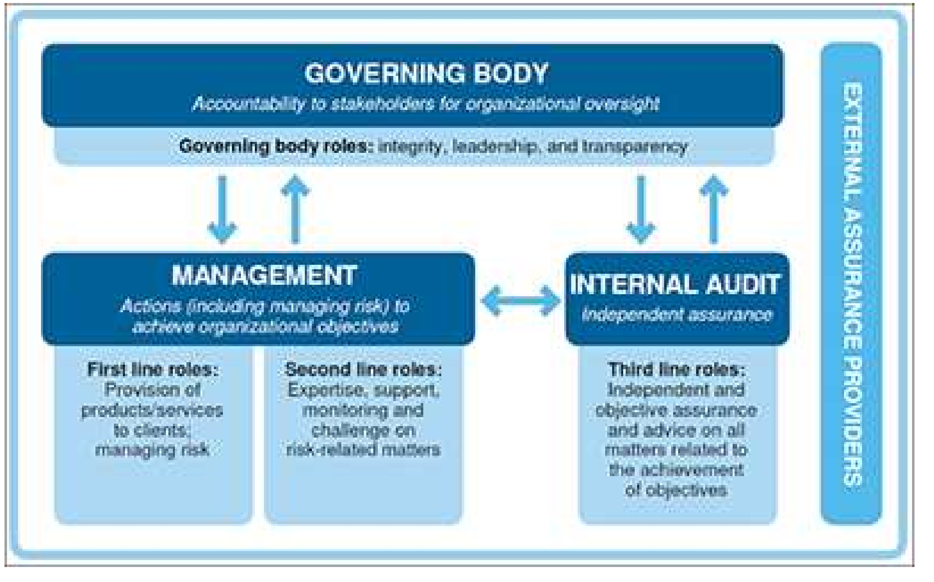
- **the first line – functions that own and manage risk.**
- **the second line – functions that oversee or specialise in risk management, compliance.**
- **the third line – functions that provide independent assurance.**

Background

The Internal Audit service for South Somerset District Council is provided by SWAP Internal Audit Services. The team's work is completed to comply with the International Professional Practices Framework of the Institute of Internal Auditors, further guided by interpretation provided by the Public Sector Internal Audit Standards (PSIAS) and the CIPFA Local Government Application Note. The work of the team is guided by the Internal Audit Charter which is reviewed annually.

Internal Audit provides an independent and objective opinion on the Authority's control environment by evaluating its effectiveness. This report summarises the activity of the Internal Audit team for the 2020/21 year.

The position of Internal Audit within an organisation's governance framework is best summarised in the Three Lines model shown below.



The Head of Internal Audit (SWAP Assistant Director) is required to provide an opinion to support the Annual Governance Statement.

Annual Opinion

On the balance of our 2020/21 audit work for South Somerset District Council, I am able to offer a **Reasonable Assurance** opinion in respect of the areas reviewed during the year.

Just as in more normal times, audit work has been planned to ensure that sufficient assurance will be available to support the annual opinion. The professional requirements of PSIAS have remained unchanged and in line with these, new audit priorities to cover the risks from the impact of COVID-19 have been agreed throughout the year and that work supports the annual opinion.

The additional audits performed to carry out assurance work on new risks associated with the Covid-19 emergency response were:

- Covid-19 Support/Advice
- Grant Funding Schemes Assurance for Local Authorities (Risk Assessment)
- Local restriction Grant Support
- Grant Support – Bank detail checks
- Business Grants - Post Assurance Review
- Compliance & Enforcement Grant
- Fraud Risk – Impact of Covid-19

It has been agreed to defer some of the audit work to 2021/22 and this has been reported throughout the year to the Audit Committee. Where relevant, management provided assurance to the Audit Committee on progress against some of these deferred pieces of work, namely Council Tax and Business Rates.

The following are considered key pieces of audit work that support the annual opinion on the overall adequacy and effectiveness of the organisation's governance, risk management and control:

The Head of Internal Audit (SWAP Assistant Director) is required to provide an opinion to support the Annual Governance Statement.

Annual Opinion

- *Cyber Security Framework Review*
- *Project Governance – Regeneration Projects*
- *Health & Wellbeing*
- *Income Generation*
- *Budget Planning and Monitoring*
- *Transformation Closedown*
- *Ethical Governance*
- *Risk Management*
- *Commercial Investments*
- *ICT Governance and Risk Review*

Throughout a challenging year, we have tried to ensure a balance between providing direct assistance to the Council and maintaining a continuum of audit work. We are pleased to report we have achieved this, although it must be recognised coverage is not comparable to previous or 'normal' years. The table at Figure 1 below attempts to capture our audit coverage this year, mapped against the Authority's key risks. It must be noted that it is not possible to cover all key risks in any one year but to provide coverage over the medium term.

Internal audit coverage should be aligned to key corporate priorities and key corporate risks.

Audit Coverage by Corporate Risk

Figure 1: Audit Coverage by Corporate Risk

Table Key	Reasonable internal audit coverage 2020-21	Partial internal audit coverage 2020-21	No internal audit coverage 2020-21

Corporate Risk	Coverage
ST01/F01 – Balanced Budget	
ST02/FS01 - Transformation	
ST03/GL01 – Government Legislation	
ST04/SC01 – Staff Retention	
ST07 – Civil Emergencies	
F02 – Overspend/underachieve Income	
F03 – Missed funding	
F04 – Integrity of Finance System	
F05 – Fraudulent Actions	
F06 – Borrowing/Investments	
F07 – Reserves	
F08 – Partnerships	
GL02 – Officer Inducement	
GL03 – Data breaches/losses	
GL05 – Corporate Procedures	
GL06 – Statutory Duties	
GL07 – Decisions	

Corporate Risk	Coverage
HS01 – Threats to staff	
HS02 – Incident/Accidents public space	
HS03 – Incident/Accident SSDC Premises	
HS05 – Exposure to Hazardous Materials	
HS06 – Accidents through maintenance	
SC02 – Quality of work	
SC03 – Current & Future work requirements	
PP01 – Initiation of Projects	
PP02 – Execution of Projects	
PP03 – Knowledge on Projects	
FS02 – Programme Budgets	
FS03 – Engagement in NWOW	
FS04 – Customer buy in	
FS06 – Member Portal	
FS07 – NWOW not enabled	
D01 – Digital Strategy not embedded	
D02 – Digital Strategy Outcomes	

Summary of Audit Work 2020/21

Definitions of Corporate Risk

High Risk
Issues that we consider need to be brought to the attention of both senior management and the Audit Committee.

Medium Risk
Issues which should be addressed by management in their areas of responsibility.

Low Risk
Issues of a minor nature or best practice where some improvement can be made.

Significant Corporate Risks

Our audits examine the controls that are in place to manage the risks that are related to the area being audited. We assess the risk at a 'Corporate' level once we have tested the controls in place. Where the controls are found to be ineffective and the 'Corporate risk' as 'High' these are brought to the Audit Committees attention. For those audits which have reached report stage through the year, we have assessed the following risks as 'High'.

Review Name / Risks
No risks identified as High during period.

Summary of Limited Assurance Audits

Audit Name	Risk Rating	Priority Findings		
		1	**2**	**3**
Project Governance - Regeneration Projects	Medium	0	3	2
Homelessness	Medium	0	3	2
Income Generation / Service Improvements	Medium	0	2	1

Note all these audits have been reported throughout 2020-21 to the Audit Committee.

Summary of Audit Work 2020/21

At the conclusion of an audit assignment each review is awarded an Audit Assurance Opinion:

- **Substantial - A sound system of governance, risk management and control exists.**
- **Reasonable - Some issues, non-compliance or scope for improvement were identified which may put at risk the achievement of objectives.**
- **Limited - Improvement is required to the system of governance, risk management and control to effectively manage risks to the achievement of objectives.**
- **None - The system of governance, risk management and control is inadequate to effectively manage risks to the achievement of objectives.**

Summary of Audit Opinion

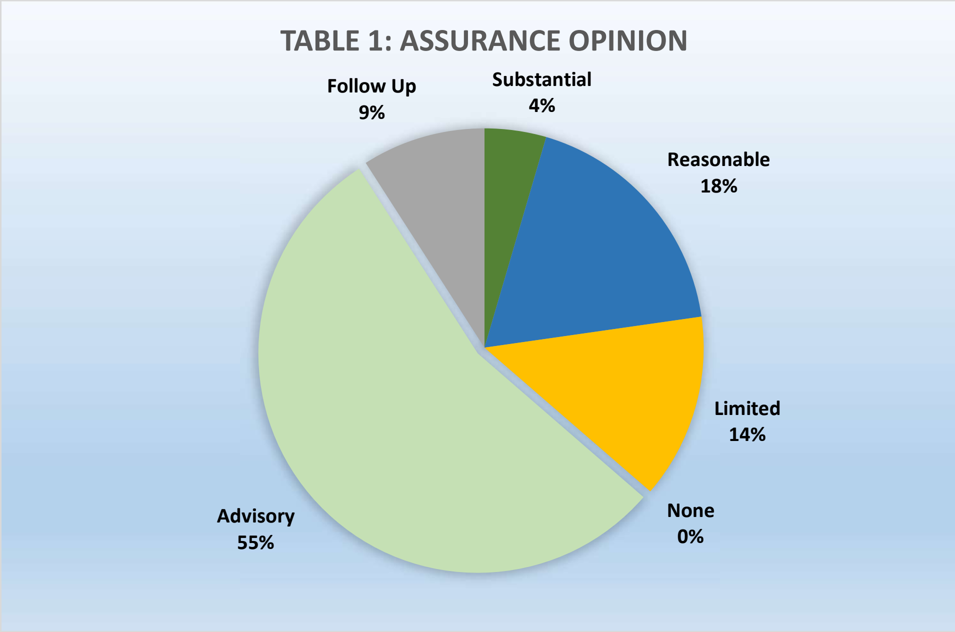


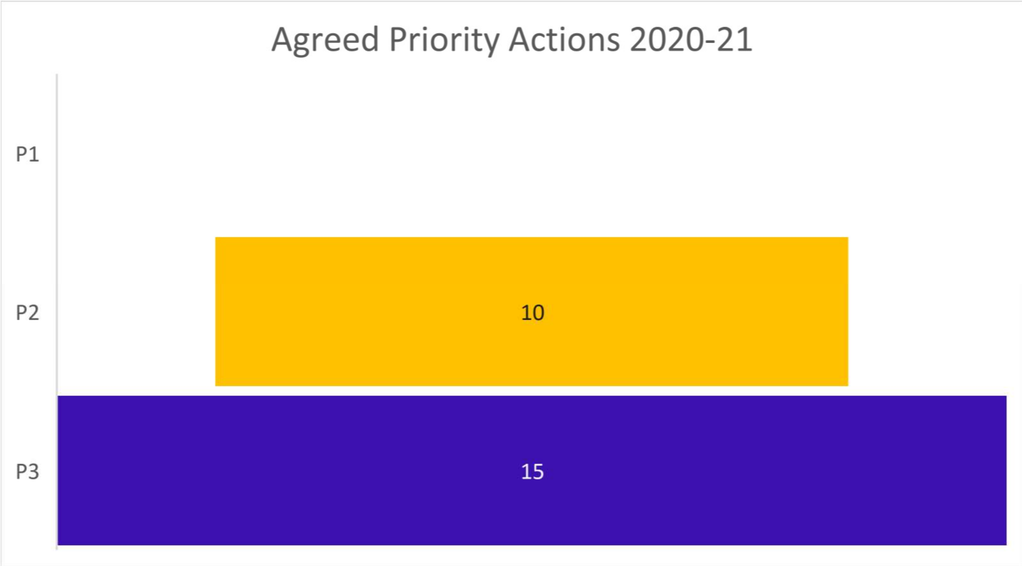
Table 1 above indicates the spread of assurance opinions across our work during the past year (2020-21). Due to Covid-19 more time has been spent on 'Advisory' work.

Summary of Audit Work 2020/21

SWAP Performance - Summary of Audit Actions by Priority

We rank our actions on a scale of 1 to 3, with 3 being medium or administrative concerns to 1 being areas of major concern requiring immediate corrective action

Priority Actions



Note: Does not include actions from Cyber Security Review and ICT Governance Risk Scope Review. Outcomes from these reviews were not assessed on the priority scoring system, but rather to highlight areas that were fully compliant, requires further work or requires immediate attention.

Added Value

Extra work that goes beyond the standard expectations and provides something that is beneficial to the customer for little or no extra cost.

Added Value

Throughout the year, SWAP strives to add value wherever possible i.e. going beyond the standard expectations and providing something 'more' while adding little or nothing to the cost.

Benchmarking

During the year we have provided benchmarking data across either the SWAP partnership or the wider reach of the Local Authority Chief Auditors Network (LACAN) for:

- Baseline Assessment of Fraud Maturity Comparison
- Risk Management Maturity Benchmarking
- Covid-19 Grant Controls

Members Training

During November we ran a free Audit Committee Members training event to provide an overview of the role of the Audit Committee as well as 'hot topics' that should be on Audit Committee radars.

News Roundup

We produce a monthly newsletter that provides information on topical areas of interest for public sector bodies. During the early stages of Covid-19 we increased the frequency of our newsflash to weekly/Fortnightly to provide relevant information.

Innovations and Enhancements to our Audit Process

During this exceptional year, we have taken the opportunity to implement and introduce a number of innovations and enhancements to our audit process. This has included:

- Introducing the concept of 'Agile Auditing' to our audit process. With increased collaboration and a joint commitment with the service under review, it is possible to complete audits faster and more efficiently. We have used this concept to complete a number of audits this year.

Added Value

Extra feature(s) of an item of interest (product, service, person etc.) that go beyond the standard expectations and provide something more while adding little or nothing to its cost.

Added Value

- With the help of SWAP's two newly appointed Data Analysts, we are looking to include analysis of data as part of our auditing wherever possible. This allows us not only the opportunity to test whole populations of data, but where this is not possible or appropriate, to be able to use data analytics to target our testing in a more effective manner.

- SWAP's Counter Fraud Team has also facilitated access to counter fraud intelligence resources and issued alerts and newsletters to key officers in the Council.

- Introduced a new one-page audit report, that summarises all the key messages of the audit on one page for ease of consumption as well as increasing impact. Feedback on the report style has again been extremely positive.

- Introduced a new continuous audit planning and risk assessment process.

Plan Performance 2020/21

Internal audit is responsible for conducting its work in accordance with the Code of Ethics and Standards for the Professional Practice of Internal Auditing as set by the Institute of Internal Auditors and further guided by interpretation provided by the Public Sector Internal Audit Standards (PSIAS).

SWAP Performance

SWAP's performance is subject to regular monitoring and review by both the SWAP Board of Directors and the Owners Board. The respective outturn performance results for SSDC for the 2020/21 year are as follows:

Performance Target	Average Performance
Audit Plan – Percentage Progress Final, Draft and Discussion > 90% In progress/Review Yet to complete	 90% 10% 0%
Customer Satisfaction Questionnaire Feedback Target > 95%	100%

SWAP work is completed to comply with the International Professional Practices Framework (IPPF) of the Institute of Internal Auditors, further guided by interpretation provided by the Public Sector Internal Audit Standards (PSIAS) and the CIPFA Local Government Application Note.

Under these standards we are required to be independently externally assessed at least every five years to confirm compliance to the required standards. SWAP was recently assessed in February 2020 and confirmed that we are in conformance to PSIAS.

Attribute Standard 1300 of the IPPF requires Heads of Internal Audit to develop and maintain a Quality Assurance and Improvement Programme (QA&IP). Standard 1310 continues this dual aspect by stating that the programme must include both internal and external assessments. This acknowledges that high standards can be delivered by managers, but it also implies that improvements can be further developed when benchmarking is obtained from outside the organisation and the internal audit function. Following our External Assessment, we have pulled together our QA&IP and included additional improvements and developments identified internally that we want to make, as aligned to SWAP's Business Plan. The QA&IP is a live document and will be regularly reviewed by the SWAP Board to ensure continuous improvement and delivery on our actions.

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
FINAL									
Fraud, Corruption and Governance	Boden Mill & Chard Regeneration Scheme Accounts Review	Q1	Final	Advisory	0	0	0	0	
Fraud, Corruption and Governance	**New:** Growth Deal Capital Expenditure Certification	Q1	Final	Advisory	0	0	0	0	
Fraud, Corruption and Governance	Yeovil Cemetery & Crematorium Annual Accounts Controls Assurance	Q1	Final	Advisory	0	0	0	0	
Covid-19 Support	**New:** Covid-19 Support/Advice	Q1	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	Project Governance - Regeneration Projects	Q1	Final	Limited	5	0	3	2	
Follow Up	Combined Follow up	Q1	Final	Follow up	0	0	0	0	
Covid-19 Support	**NEW:** Grant Funding Schemes Assurance for Local Authorities (Risk Assessment)	Q1	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	**NEW:** Health & Wellbeing	Q2	Final	Reasonable	2	0	0	2	
Operational	Homelessness	Q2	Final	Limited	5	0	3	2	
ICT	Cyber Security Framework Review	Q3	Final	Advisory	20 key Control areas reviewed. Reported separately to Audit Committee.				
Covid-19 Support	**NEW:** Local restriction Grant Support	Q3	Final	Advisory	0	0	0	0	Support work

Plan Performance 2020/21

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
Governance Fraud & Corruption	Income Generation Service Improvements	Q3	Final	Limited	3	0	2	1	
Key Control	Budget Planning and Monitoring	Q3	Final	Reasonable	2	0	0	2	
ICT	ICT Governance and Risk Scope Review	Q3	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	**NEW:** Covid-19 Grant Processing Support	Q4	Final	Advisory	0	0	0	0	
Covid-19 Support	**NEW:** Grant Support – Bank detail checks	Q4	Final	Advisory	0	0	0	0	
Governance Fraud & Corruption	**NEW:** Council Baseline Assessment of maturity for Fraud	Q4	Final	Advisory	0	0	0	0	
Covid-19 Support	**NEW:** Business Grants - Post Assurance Review	Q4	Final	Substantial	0	0	0	0	
Key Control	Creditors	Q4	Final	Reasonable	3	0	1	2	
Governance Fraud & Corruption	Ethical Governance	Q4	Final	Reasonable	5	0	1	4	
Governance Fraud & Corruption	**NEW:** Compliance & Enforcement Grant	Q4	Final	Advisory	0	0	0	0	
Draft									
Transformation	Transformation closedown	Q2	Draft						
Follow Up	Information Governance GDPR Follow Up	Q4	Draft						
Operational	S106 & CIL	Q4	Draft						

Plan Performance 2020/21

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
Governance Fraud & Corruption	**NEW:** Fraud Risk – Impact of Covid-19	Q4	Drafting						
In Progress									
Governance Fraud & Corruption	Commercial Investments	Q3	In progress						
Governance Fraud & Corruption	Risk Management	Q4	In Progress						
Governance Fraud & Corruption	**NEW:** Fraud Risk Assessment	Q4	In Progress						
Deferred or Removed									
Transformation	Civica Digital Systems Review	Q2			Combined with Transformation Close down				
Governance Fraud & Corruption	Somerset Districts Cooperation/collaboration FOLGIS	Q4			**NEW:** Covid-19 Support/Advice **NEW:** Grant Funding Schemes Assurance for Local Authorities (Risk Assessment)				
Governance Fraud & Corruption	Climate Change	Q4							
ICT	Digital Strategy & Transformation	Q3			Pushed back due ICT audits bottleneck. Replaced by Health & Wellbeing				
Governance Fraud & Corruption	Yeovil Innovation Centre (YIC) Phase 2	Q4			**NEW:** Local restriction Grant Support Q3 **NEW:** Grant Support – Bank detail checks Q4 **NEW:** Council Baseline Assessment of maturity for Fraud **NEW:** Fraud Risk Assessment				
Key Control	Council Tax & NNDR	Q4							

Plan Performance 2020/21

Audit Type	Audit Area	Qtr	Status	Opinion	No of Rec	1 = Major	↔	3 = Minor	Comments
						Recommendation			
						1	2	3	
Key Control	Housing Benefits	Q4							**NEW:** Fraud Risk – Impact of Covid-19 **NEW:** Covid-19 Grant Processing Support Q4 **NEW:** Compliance & Enforcement Grant Management provided an update to Audit Committee in March for Housing Benefits and CTax. Procurement – Leisure is earmarked for Q1 2021-22
Governance Fraud & Corruption	Procurement – Leisure Contract	Q4							

South Somerset District Council

2020/21 Treasury Management Mid-Year Performance Report and Strategy Update

Executive Portfolio Holder:	Peter Seib, Finance and Legal Services
Director:	Nicola Hix, Support Services & Strategy
Section 151 Officer:	Karen Watling, Interim Section 151 Officer
Lead Officer:	Paul Matravers, Lead Specialist - Finance
Contact Details:	Paul.matravers@southsomerset.gov.uk or 01935 462275

Purpose of the Report

1. To review the treasury management activity and the performance against the Prudential Indicators for the 2020/21 financial year as prescribed by the CIPFA Code of Practice and in accordance with the Council's Treasury Strategy, Annual Investment Policy and Treasury Management Practices.

Forward Plan

2. This report appeared on the Audit Committee Forward Plan with an anticipated Committee date of 27th May 2021.

Public Interest

3. The Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services Code of Practice requires the Council to approve an annual Treasury Management Strategy and, report treasury performance mid-year and at the year end.

Recommendations

4. The Audit Committee is recommended to:
   - Note the Treasury Management Activity for the 2020/21 financial year;
   - Note the position of the individual prudential indicators for the 2020/21 financial year;
   - Note the outlook for the investment performance in 2020/21;
   - Note the Council operated within all of the Prudential Indicators during 2020/21;
   - Recommend the 2020/21 Treasury Management Activity Report to full Council.

Background

5. Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year and, as a minimum, produce a six month and annual treasury

outturn report. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code. The Council reports six monthly to Full Council against the strategy approved for the year. The scrutiny of treasury management policy, strategy and activity is delegated to the Audit Committee.

6. Full Council approved the Council's 2020/21 Treasury Management Strategy on 6 February 2020. The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk remains central to the Council's Treasury Management Strategy.

7. The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Council's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 6 February 2020.

8. Overall responsibility for treasury management remains with the Council. The day to day treasury management operation is delegated to the S151 Officer and is undertaken by the Finance function which is part of the Support Services directorate. No treasury management activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives.

9. This report provides information on the performance of the Council's Treasury Investments in 2020/21. The performance of the Council's Commercial Investments, which are part of the Commercial Strategy, are not included in this report.

South Somerset District Council

Treasury Management Position - Summary

10. The treasury management position at 31st March 2021 and the change during the year is shown in the table below.

	31/03/2020 Balance £000's	Net Movement £000's	31/03/2021 Balance £000's
Long-term borrowing	-	-	-
Short-term borrowing	(79,500)	(18,500)	(98,000)
Total Borrowing	**(79,500)**	**(18,500)**	**(98,000)**
Long-term Investments	2,000	-	2,000
Short-term Investments	8,000	(8,000)	-
Cash and Cash Equivalents	22,430	1,550	23,980
Total Investment	**32,430**	**(6,450)**	**25,980**
Net Position	**(47,070)**	**(24,950)**	**(72,020)**

11. External borrowing has increased during the year, reflecting the financing of planned capital expenditure, particularly in respect of investment property acquisition. In line with treasury advice, the Council continues to utilise short term borrowing, which is flexible and keeps our borrowing costs low. The projected value of borrowing as at 31 March 2021 was reported to Audit Committee in January 2021 in the Annual Treasury Management Strategy report.

12. The amount of external borrowing is partially dependent on the commercial property purchases that are made in the financial year, with cash flow requirements also dictating the level of borrowing. Short term borrowing continues to be the best option to meet the financing requirement.

13. The S151 Officer has requested a piece of work be carried out by the Council's treasury advisors on alternative borrowing options. This is required in light of the revision to the lending criteria for HM Treasury's PWLB lending facility, which has historically been seen as the preferred option for local authority borrowing. The lending criteria which came into place in November 2020 has meant that the PWLB may not be available as a financing option in the future.

14. The work on alternative borrowing options is in its infancy, with a report detailing the options anticipated to be completed by the end of the May. The report will be presented to this committee at a future date once the report has been reviewed by senior officers.

15. An amendment to the 2021/22 borrowing strategy, which was approved by Full Council in February 2021, may be required if the Treasury advisors report recommends alternative borrowing options which are not currently included in the

approved borrowing strategy. If needed, the revised borrowing strategy will be brought to this committee for scrutiny and approval.

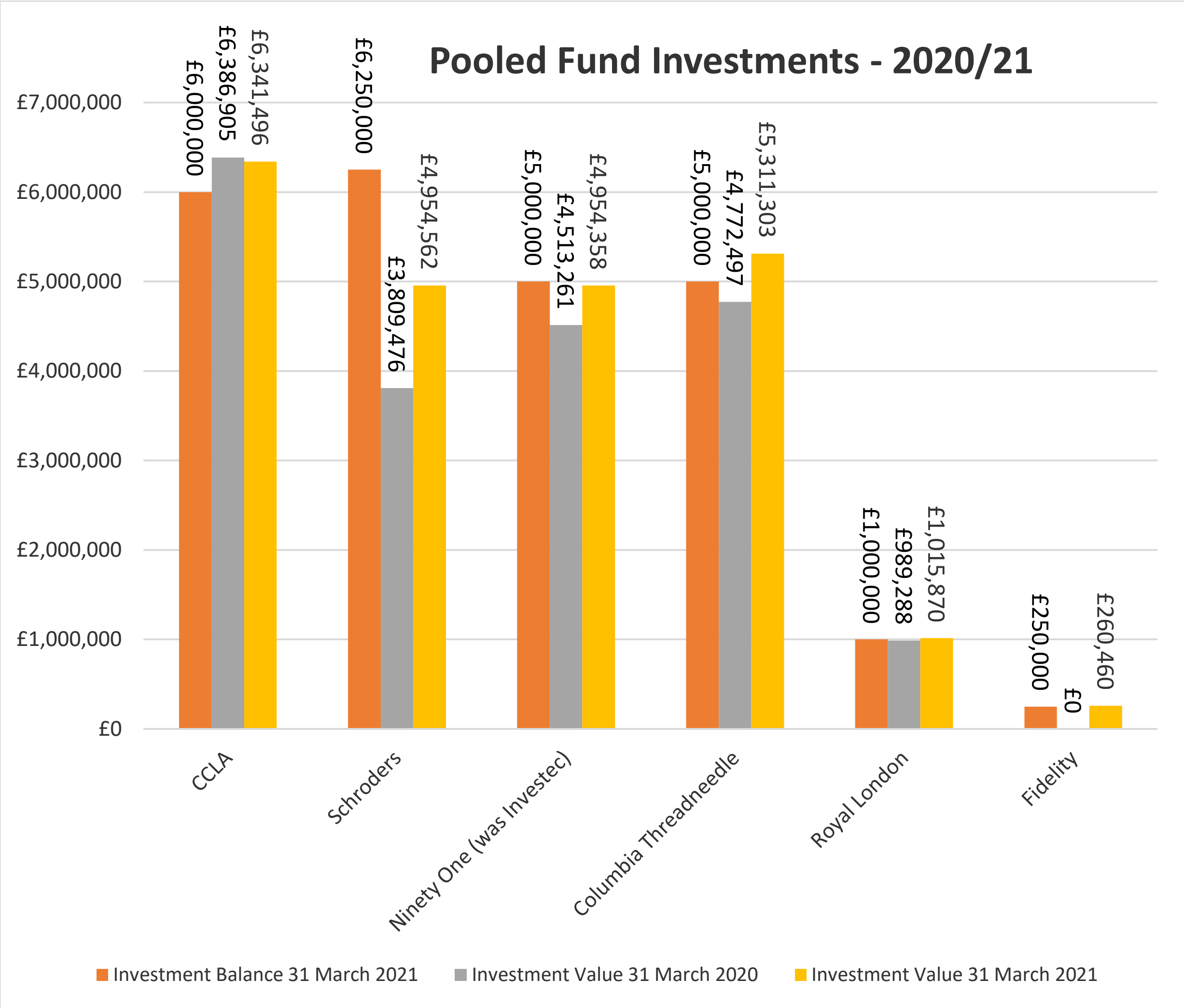
16. As well as the request to report on the borrowing options available, ongoing dialogue is held with the Council's Treasury advisors on the best options for borrowing at present. The current advice being to continue to borrow short term at present. However, the Council may utilise long term borrowing (as part of the current strategy) in 2021/22 if it is deemed the best option, which will also remove an element of interest rate risk.

Investment Activity

17. The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. During 2020/21, the Council's investment balance ranged between £26 million and £86 million. The balance of £86m was due to the funding received from Central Government in respect of the Business Grants in early April 2020.

18. Both the CIPFA Code and Government guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

19. The Council's best performing investments continue to be the investments in the Pooled Funds (Strategic Investments). Details of the investment balance as at 31 March 2021 and the value of each investment at the same date is detailed in the chart below.



Note: Pooled fund investments are revalued at the end of the financial year to reflect the fair value of the investment; the third bar in the graph signifies this value and details the investment value as at 31 March 2021. The first bar represent the investment balance in each fund at that date.

Pooled Fund Investments 2020/21

20. The table below includes the opening and closing investment balances for each pooled fund investment. The investment fair value signifies the individual value of the investments after the year end revaluation.

South Somerset District Council

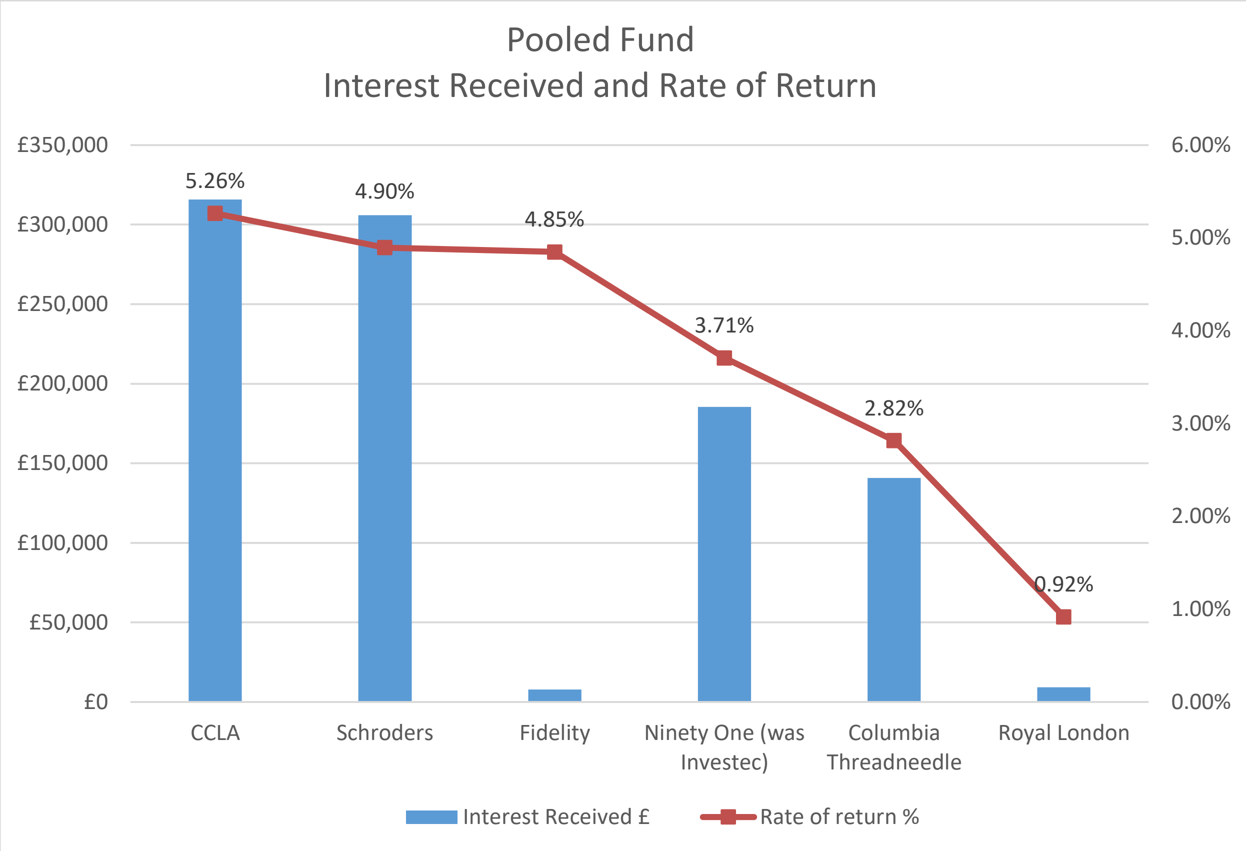
Investment Type	Investment Balance 01/04/2020 £000's	Investment Balance 31/03/2021 £000's	Investment Balance Change £000's	Investment Value 01/04/2020 £000's	Investment Value 31/03/2021 £000's	Investment Value Change £000's
CCLA	£6,000	£6,000	£0	£6,387	£6,341	(£46)
Schroders	£6,250	£6,250	£0	£3,809	£4,955	£1,146
Investec	£5,000	£5,000	£0	£4,513	£4,954	£441
Colombia Threadneedle	£5,000	£5,000	£0	£4,772	£5,311	£539
Royal London	£1,000	£1,000	£0	£989	£1,016	£27
Fidelity	£0	£250	£250	£0	£260	£260
Total	**£23,250**	**£23,500**	**£250**	**£20,470**	**£22,837**	**£2,367**

21. The Council increased it investments in pooled funds by £0.25m in 2020/21 making the investments £23.5m as at 31 March 2021. An investment of £250k was made in the Fidelity Global Enhanced Income Fund, this investment is seen as an initial investment and it is anticipated that further amounts (£250k) will be invested in the fund if it continues to provide positive capital growth and income returns.

22. The Council has investments in bond, equity, multi-asset and property funds. During the initial phase of the pandemic in March 2020, the sharp falls corporate bond and equity markets had a negative impact on the value of the Council's pooled fund holdings and was reflected in the 31st March 2020 fund valuations with most funds registering negative capital returns over a 12-month period. Since March 2020 there here has been improvement in market sentiment which is reflected in an increase in the capital values in five of the six funds, as demonstrated in the final column of the above table.

23. It should be noted that the £2.37m increase in the capital value of the investments will not have an impact on the General Fund as the Council is using the alternative fair value through profit and loss (FVPL) accounting and defers the funds' fair value losses (and gains) to the Pooled Investment Fund Adjustment Account until 2023/24.

24. The income generated from these investments in 2020/21 and the rate of return is detailed in graph and table below.



Fund	Interest Received £	Rate of return %
CCLA	£315,824	5.26%
Schroders	£305,962	4.90%
Fidelity	£7,870	4.85%
Ninety One (was Investec)	£185,393	3.71%
Columbia Threadneedle	£140,772	2.82%
Royal London	£9,187	0.92%
Total	**£965,009**	**4.12%**

25. Similar to many other property funds, dealing (i.e. buying or selling units) in the CCLA Local Authorities' Property Fund was suspended by the fund in March 2020 and lifted in September. There was also a change to redemption terms for the fund; from September 2020 investors are required to give at least 90 calendar days' notice for redemptions.

26. Pooled funds have no defined maturity date, but are available for withdrawal after a notice period. Their performance and continued suitability in meeting the Council's investment objectives is regularly reviewed. Strategic fund investments are made in the knowledge that capital values will move both up and down; but with the confidence that over a three to five-year period total returns will exceed cash interest rates.

27. In light of their strong performance and the Council's latest cash flow forecasts, there was a small increase in the investment in these funds. The investment (Fidelity) has proved to be successful with the income return being above 4.50% in year. A good return on other pooled fund investments was also achieved in the 2020/21 financial year. The capital value of the investments has increased and there are positive signs that the capital value of the investments has been maintained in the first month of 2021/22.

28. The investment strategy approved in the 2021/22 Treasury Management Strategy Statement recommended that the Council maintains its investments in the secure and higher yielding asset classes given the increasing risk and very low returns from short-term unsecured bank investments.

29. The graph above and table detailing interest received, and the rate of return on investments demonstrates that the approved policy has met the objectives of the investment strategy. It is anticipated that the level of strategic (long-term) investments will remain in the region of £24m in 2021/22, with the possibility of increasing these investments, if cash flow permits, in line with the Council's overall Financial Strategy and income generation targets.

30. The diversification into strategic investments represents a continuation of the strategy adopted in 2017/18. The Council's Treasury advisors have indicated that a maximum exposure to this investment type should be limited to £30m.

31. The revised Financial Strategy and Medium Term Financial Plan reflects the current economic situation as a result of Covid-19, revisions to the income target for Treasury Management investments will be incorporated if required. Any potential changes to the Treasury Management Strategy and policy due to the revised Financial Strategy and MTFP will be brought to Audit Committee.

Interest Rates 2020/21

32. As detailed in the Arlingclose external context provided in Appendix A, the start of the financial year saw many central banks cutting interest rates as lockdowns caused economic activity to grind to a halt. The Bank of England cut Bank Rate to 0.1% and the UK government provided a range of fiscal stimulus measures. Rates were held at 0.1% throughout the year but the bank extended its Quantitive Easing programme by £150 billion to £895 billion at its November 2020 Meeting.

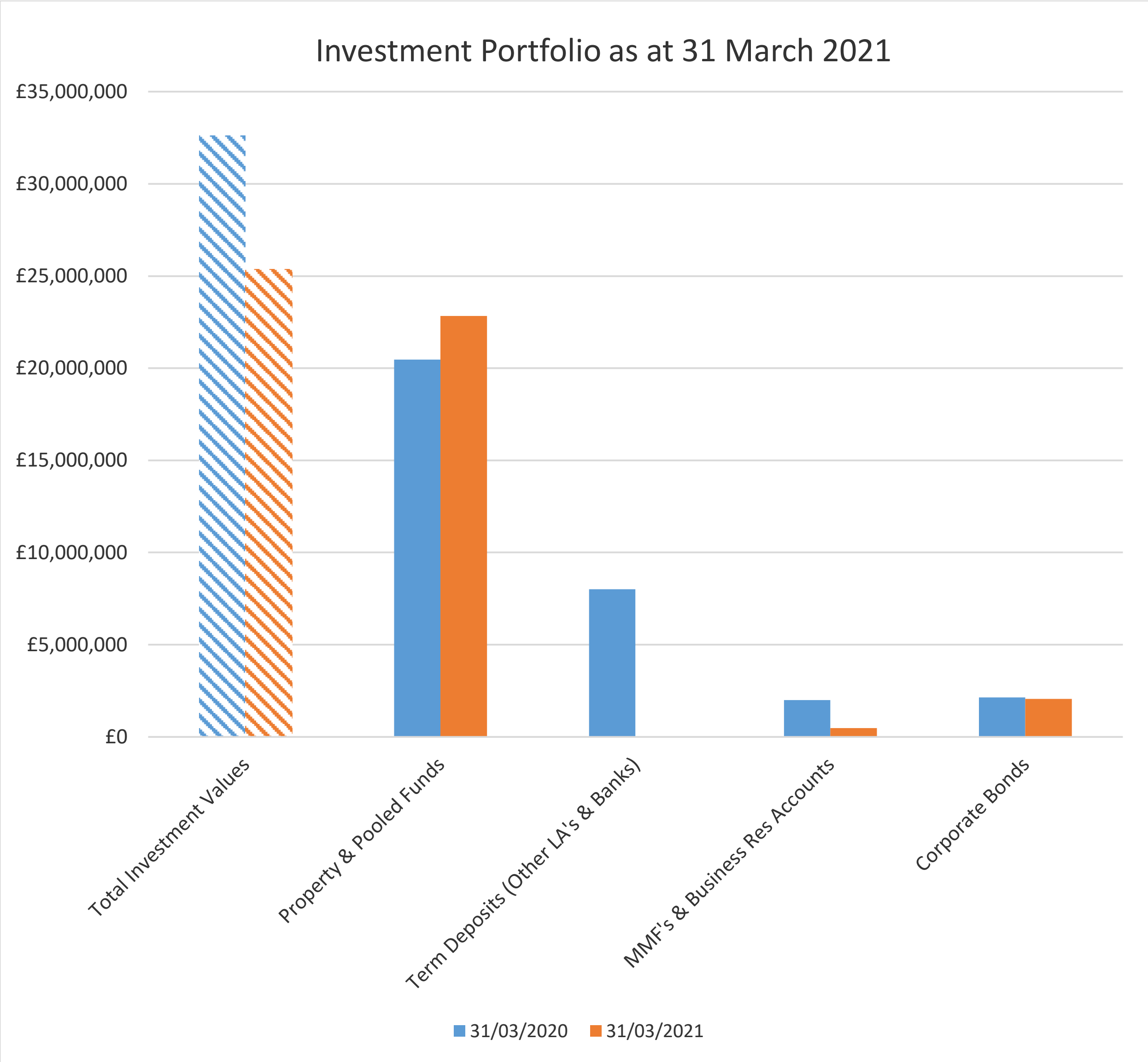
33. The Arlingclose central case assumes the bank rate will remain at 0.10% until at least June 2024. The latest economic and interest rate forecast (March 2021) from

Arlingclose states that whilst the central case assumes no change to the base rate for a significant period. It also states that the risks of a Bank Rate cut over the medium term have reduced further.

	Jun-21	Sep-21	Dec-21	Mar-22	Jun-22	Sep-22	Dec-22	Mar-23	Jun-23	Sep-23	Dec-23	Mar-24	Jun-24	Average
Official Bank Rate														
Upside risk	0.00	0.15	0.15	0.15	0.15	0.30	0.30	0.30	0.30	0.30	0.30	0.30	0.30	**0.23**
Arlingclose Central Case	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10	0.10
Downside risk	-0.10	-0.10	-0.15	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	-0.20	**-0.18**

Investment Portfolio – Values and Returns

34. The graph below provides a snapshot of the Council's portfolio of investments at the end of the 2020/21 financial year, in comparison to the previous year end position.



35. The table below provides additional information on the actual value of investments at the start and end of the 2020/21 financial year:

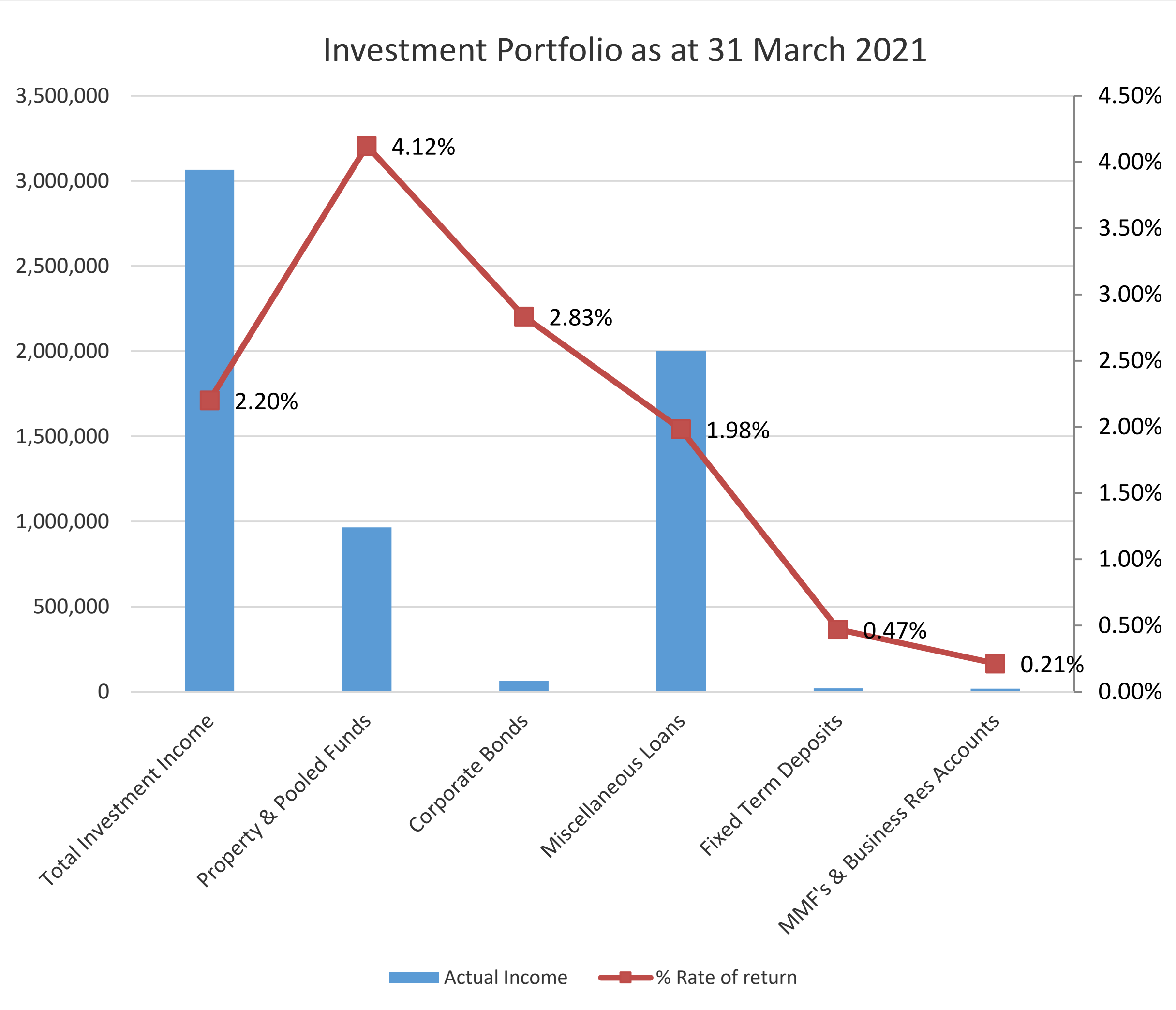
Investment type	**Investment Value as at 31/03/2020**	**Investment Value as at 31/03/2021**	**Actual Income**	**% Rate of return**
Property & Pooled Funds	20,471,426	22,838,048	965,009	4.12%
Money Market Funds & Business Reserve Accounts	2,000,000	480,000	18,126	0.21%
Term Deposits (Other LAs & Banks)	8,000,000	0	20,116	0.47%
Corporate Bonds	2,129,992	2,060,491	62,658	2.83%
Total Investment Values	**32,601,418**	**25,378,539**	**1,065,909**	**2.77%**

36. The types of investment that the Council held at the 31 March 2020 and 31 March 2021 has changed. The policy of investing in higher yielding, long term strategic investments have resulted in a large portion of the Council's investment being concentrated in the pooled and property fund investment type. Pooled and property fund investments amounted to 90% of the investment portfolio as at 31 March 2021 (66% as at 31 March 2020). The reduction in the term deposits was due to the low rates of return associated with this investment that were seen for a significant period of the financial year. The cashflow fluctuations that were experienced during the year also resulted in less cash being available for term deposit investments.

37. The Council continues to work closely with Arlingclose on the investment diversification and portfolio mix, Arlingclose are comfortable with the percentage of investment that the Council holds in pooled and property funds but has suggested a maximum exposure of £30m. The Council continually monitors the performance of the property and pooled funds and is able to withdraw funds at short notice if the fund performance were to deteriorate. Equally, the Council may borrow short term to manage cash flow variations if necessary.

Returns achieved in 2020/21

38. The returns are shown in the graph and table below:



Investment type	Actual Income £	Rate of return %
Property & Pooled Funds	965,009	4.12%
Miscellaneous Loans	1,999,490	1.98%
Fixed Term Deposits	20,116	0.47%
Corporate Bonds	62,658	2.83%
Money Market Funds & Business Reserve Accounts	18,126	0.21%
2020/21 Treasury Investment Income	**3,065,399**	**2.20%**
2020/21 Treasury Income Budget	**1,947,510**	
Surplus /(Deficit)	**1,117,889**	

39. The table above shows investment income for the year compared to the budget. The figures show a significant surplus over budget of £1,117,889. The original treasury management budget of £1,947,510 was derived by forecasting an average rate of return of 1.86% based on an average investment portfolio of £50m.

40. The surplus over budget is as a result of a number of factors, the main factors being:
    a. Additional interest received due to additional investment into long term strategic investments.
    b. A new loan for service purposes has been made in year resulting in additional interest.
    c. Additional interest received from commercial investments purchased in year that are not included in the 2020/21 budget

41. The outturn position is also affected by both the amount of cash we have available to invest and the interest base rate set by the Bank of England. Balances are affected by the timing of revenue and capital income and expenditure, and the collection and distribution of council tax and business rates income.

Treasury Investments

42. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2020/21. The table below lists the investments held on 31 March 2021.

Breakdown of investments as at 31 March 2021

Date Invested	Counterparty	Nominal Amount £'000	Rate %	Maturity Date
	Corporate Bonds			
20/10/2016	Santander UK Plc	1,000	1.04	14/04/2021
10/11/2016	National Australia Bank	1,000	1.10	10/11/2021
	Business Reserve Accounts			
	Santander Business Reserve	480	0.18	
	Property& Pooled Funds			
	Fidelity Global Enhanced Income	250	4.85	
	Ninety One Diversified Income	5,000	3.71	
	Royal London Enhanced Cash Plus Fund	1,000	0.92	
	Schroders Income Maximiser	6,250	4.90	
	Columbia Threadneedle Strategic Bond	5,000	2.82	
	CCLA Property Fund	6,000	5.26	
	Total	**25,980**		

Note: Money Market Funds are instant access accounts so the rate displayed is a daily rate

Non-Treasury Investments

43. The definition of investments in CIPFA's revised Treasury Management Code now covers all the financial assets of the Council as well as other non-financial assets which the Council holds primarily for financial return. This is replicated in MHCLG's Investment Guidance, in which the definition of investments is further broadened to also include all such assets held partially for financial return.

The Council also held £125.93m of such investments in

- Directly Owned Property - £88.28m
- Loan to Community Organisation - £0.14m
- Loan to Local Authority Partnership - £4.34m
- Loan for Commercial Activities - £33.17m

Borrowing

44. The Council's primary objective when borrowing has been to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required, with flexibility to renegotiate loans should the Council's long-term plans change being a secondary objective.

45. The table below summarises the external borrowing position for 2020/21. It details the opening position in respect of external loans, loans repaid, new loans, the average interest rate and the year-end position.

	Amount £'000	**Average Interest Rate %**
External Loans as at 1 April 2020	**79,500**	**0.86**
New Loans	160,000	0.31
Loans Repaid	(141,500)	
Total External Loans as at 31 March 2021	**98,000**	

46. In keeping with these objectives, new borrowing was kept to a minimum, however external borrowing increased from £79.5m to £98m. This strategy enabled the Council to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

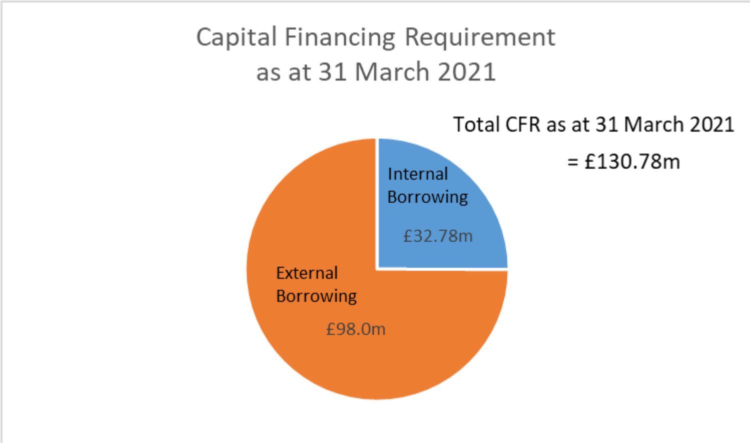
47. Details of the borrowing are included in the table below.

Lender	Date Borrowed	Repayment Date	No of Days	Interest Rate	Amount	2020/21 Interest	Total Interest
Tendring District Council	19/03/2021	21/06/2021	94	0.10%	1,000,000	36	258
Cornwall Council	17/04/2020	16/04/2021	364	1.75%	10,000,000	167,329	9,973
Wychavon District Council	20/04/2020	19/04/2021	364	1.75%	5,000,000	82,945	4,986
Ryedale District Council	11/05/2020	10/05/2021	364	1.75%	1,000,000	15,582	997
London Borough of Wandsworth	19/03/2021	19/01/2022	306	0.45%	10,000,000	1,603	8,384
Great Yarmouth Borough Council	20/10/2020	20/07/2021	273	0.20%	2,000,000	1,786	1,496
Runnymede Borough Council	20/10/2020	20/08/2021	304	0.23%	3,000,000	3,081	2,499
Mid Devon District Council	20/10/2020	20/07/2021	273	0.20%	3,000,000	2,679	2,244
Police & Crime Commissioner For Gloucestershire	20/10/2020	20/04/2021	182	0.15%	3,000,000	2,010	1,496
Northern Ireland Housing Executive	20/10/2020	20/07/2021	273	0.20%	5,000,000	4,466	1,496
Derbyshire Fire and Rescue Service	29/03/2021	29/06/2021	92	0.10%	4,000,000	33	403
Cherwell District Council	22/03/2021	19/04/2021	28	0.08%	2,000,000	44	46
Lancaster City Council	17/03/2021	19/04/2021	33	0.10%	5,000,000	205	452
West Berkshire Council	12/03/2021	21/04/2021	40	0.06%	1,000,000	33	33
Kent County Council	17/03/2021	17/05/2021	61	0.08%	5,000,000	164	836
Wokingham Borough Council	19/03/2021	21/06/2021	94	0.08%	5,000,000	142	1,288
East London Waste Authority	22/03/2021	22/04/2021	31	0.08%	2,000,000	44	68
Nottingham City Council	22/03/2021	22/04/2021	31	0.09%	4,000,000	99	136
Derry City and Strabane District Council	24/03/2021	30/04/2021	37	0.08%	2,000,000	35	61
Nottingham City Council	29/03/2021	29/06/2021	92	0.08%	6,000,000	39	1,512
Cambridge City Council	29/03/2021	29/06/2021	92	0.08%	5,000,000	33	1,260
Blaenau Gwent County Borough Council	26/03/2021	28/04/2021	33	0.08%	5,000,000	66	181
Flintshire County Council	26/03/2021	19/04/2021	24	0.08%	2,000,000	26	53
Solihull Metropolitan Borough Council	26/03/2021	30/04/2021	35	0.08%	1,000,000	13	38
West Midlands Combined Authority	31/03/2021	25/05/2021	55	0.06%	6,000,000	10	271
				Total	**98,000,000**	**282,504**	**40,465**

48. With short-term interest rates remaining much lower than long-term rates, the Council considered it cost effective in the near term to use internal resources in parallel with short-term loans.

49. The Council's underlying need to borrow is defined as its 'Capital Financing Requirement (CFR)'. The CFR was £95.5m million at the beginning of 2020/21. Capital expenditure during 2020/21 was funded through a combination of capital receipts, revenue reserves, external contributions (e.g. S106 receipts) and borrowing. As a result, the borrowing requirement (CFR) has increased to £130.7 million. However, we have followed a strategy of using our cash reserves to finance this borrowing requirement in the short term – known as "internal borrowing" – as short term investment returns foregone are currently lower than longer term borrowing rates.

Borrowing Type	£'000	%
Internal Borrowing	£32,777	25.06%
External Borrowing	£98,000	74.94%
Total Capital Financing Requirement as at 31 March 2021	**£130,777**	



Treasury Management Indicators

50. The Authority measures and manages its exposures to treasury management risks using the following indicators.

Security: The Authority has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit rating of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment. Unrated investments are assigned a score based on their perceived risk.

	2020/21 Target	2020/21 Actual
Portfolio average credit rating	5.0	3.2

Liquidity: The Authority has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available to meet unexpected payments within a rolling three-month period.

	2020/21 Target	2020/21 Actual
Total cash available within 3 months	£10m	£25m

Interest Rate Exposures: This indicator is set to control the Authority's exposure to interest rate risk. The upper limits on the one-year revenue impact of a 1% rise or fall in interests was:

	2020/21 Limit	2020/21 Actual
Upper limit on one-year revenue impact of a 1% change in interest rates	£200,000	£33,300

The impact of a change in interest rates is calculated on the assumption that maturing loans and investment will be replaced at current rates.

Maturity structure of borrowing: This indicator is set to control the Council's exposure to refinancing risk. The upper and lower limits on the maturity structure of borrowing will be:

Refinancing rate risk indicator	2020/21 Upper Limit %	2020/21 Lower Limit %	2020/21 Actual %
Under 12 months	100%	100%	100%
12 months and within 24 months	100%	100%	0%
24 months and within 5 years	100%	100%	0%
5 years and within 10 years	100%	100%	0%
10 years and above	100%	100%	0%

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment. Upper and lower limits are set at 100% providing full flexibility to optimise borrowing arrangements.

Principal sums invested for periods longer than a year: The purpose of this indicator is to control the Authority's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the long-term principal sum invested to final maturities beyond the period end were:

Price risk indicator	2020/21
Actual principal invested beyond year end	£2m
Limit on principal invested beyond year end	£30m

The impact of a change in interest rates is calculated on the assumption that maturing loans and investment will be replaced at current rates.

Other

CIPFA consultations: In February 2021 CIPFA launched two consultations on changes to its Prudential Code and Treasury Management Code of Practice. These follow the Public Accounts Committee's recommendation that the prudential framework should be further tightened following continued borrowing by some authorities for investment purposes. These are principles-based consultations and will be followed by more specific proposals later in the year. In the Prudential Code the key area being addressed is the statement that "local authorities must not borrow more than or in advance of their needs purely in order to profit from the investment of the extra sums borrowed". Other proposed changes include the sustainability of capital expenditure in accordance with an authority's corporate objectives, i.e. recognising climate, diversity and innovation, commercial investment being proportionate to budgets, expanding the capital strategy section on commercial activities, replacing the "gross debt and the CFR" with the liability benchmark as a graphical prudential indicator.

Proposed changes to the Treasury Management Code include requiring job specifications and "knowledge and skills" schedules for treasury management roles to be included in the Treasury Management Practices (TMP) document and formally reviewed, a specific treasury management committee for MiFID II professional clients and a new TMP 13 on Environmental, Social and Governance Risk Management.

Prudential Indicators – 2020/21

51. In February 2020, through approval of the Treasury Management Strategy Full Council approved the Prudential Indicators for 2020/21, as required by the Prudential Code for Capital Finance in Local Authorities. The Local Government Act 2003 allows local authorities to determine their own borrowing limits provided they are affordable and that every local Council complies with the Code.

Capital Expenditure: The actual capital expenditure incurred for 2020/21 compared to the revised estimate was:

	2019/20 Outturn £'000	2020/21 Revised Estimate £'000	2020/21 Outturn £'000	2020/21 Variance £'000	Reason for Variance
Approved capital schemes	65,483	31,524	41,780	10,256	Spend on Energy Projects
Total Expenditure	**65,483**	**31,524**	**41,780**	**10,256**	

Ratio of Financing Costs to Net Revenue Stream: This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

	2019/20 Outturn £'000	2020/21 Revised Estimate £'000	2020/21 Outturn £'000	2020/21 Variance £'000	Reason for Variance
Financing Costs	(966)	(77)	1,269	1,345	Additional interest on borrowing
Net Revenue Stream	15,636	15,207	15,150	(58)	
%	**-6.2%**	**-0.5%**	**7.8%**		

*figures in brackets denote income through receipts and reserves

The financing costs include interest payable and notional amounts set aside to repay debt less interest on investment income. The figure in brackets is due to investment income outweighing financing costs significantly for the Council but is relevant since it shows the extent to which the Council is dependent on investment income.

Estimates of Capital Financing Requirement: The Capital Financing Requirement (CFR) measures the Authority's underlying need to borrow for a capital purpose.

	2019/20 Outturn £'000	2020/21 Revised Estimate £'000	2020/21 Outturn £'000	2020/21 Variance £'000
Opening CFR	39,320	95,581	95,581	-
Capital Expenditure	65,482	53,752	41,781	(11,971)
Capital Receipts*	(6,820)	(8,992)	(3,274)	5,718
Grants/Contributions*	(1,881)	(231)	(2,360)	(2,129)
Minimum Revenue Provision (MRP)	(520)	(747)	(951)	(204)
Additional Leases taken on during the year	-	-	-	-
Closing CFR	**95,581**	**139,363**	**130,777**	**(8,586)**

*Figures in brackets denote income through receipts or use of revenue resources.
Total figures are rounded

Gross Debt and the Capital Financing Requirement: In order to ensure that over the medium term debt will only be for a capital purpose. The Council should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.

	2019/20 Outturn £'000	2020/21 Revised Estimate £'000	2020/21 Outturn £'000	2020/21 Variance £'000
Borrowing	79,500	126,600	98,000	(28,600)
Finance Leases	51	51	20	(31)
Total Debt	**79,551**	**126,651**	**98,020**	**(28,631)**
Capital Financing Requirement	95,581	139,363	130,777	(8,586)

Total debt is expected to remain below the CFR for the near future.

Credit Risk: The Council considers security, liquidity and yield, in that order, when making investment decisions.

Credit ratings remain an important element of assessing credit risk, but they are not a sole feature in the Council's assessment of counterparty credit risk. The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution and its sovereign
- Sovereign support mechanisms
- Credit default swaps (where quoted)
- Share prices (where available)
- Economic Fundamentals, such as a country's net debt as a percentage of its GDP
- Corporate developments, news articles, markets sentiment and momentum
- Subjective overlay

The only indicators with prescriptive values remain to be credit ratings. Other indicators of creditworthiness are considered in relative rather than absolute terms.

Actual External Debt: This indicator is obtained directly from the Council's balance sheet. It is the closing balance for actual gross borrowing plus other long-term liabilities (this represents our finance leases). This indicator is measured in a manner consistent for comparison with the Operational Boundary and Authorised Limit.

Actual External Debt as at 31/03/2021	£'000
Borrowing	98,000
Other Long-term Liabilities (Finance Leases)	
-Vehicles	20
-Photocopiers	-
Total	98,020

Authorised Limit for External Debt: This limit represents the maximum amount that the Council may borrow at any point in time during the year. If this limit is exceeded the Council will have acted ultra vires. It also gives the Council the responsibility for limiting spend over and above the agreed capital programme. A borrowing requirement was identified in year to finance the capital programme and further borrowing may be undertaken to fund the agreed plans to acquire investment properties.

	2019/20 Actual £'000	2020/21 Original Estimate £'000	2020/21 Actual £'000
Borrowing	79,500	140,000	98,000
Other Long-term Liabilities	51	20	20
Total	79,551	140,020	98,020

Operational Boundary for External Debt: The operational boundary sets the limit for short term borrowing requirements for cash flow and has to be lower than the previous indicator, the authorised limit for external debt.

Since the operational boundary is a management tool for in-year monitoring it is not significant if the operational boundary is breached on occasions due to variations in cash flow, and this is not counted as a compliance failure.

South Somerset District Council

The S151 Officer has delegated authority, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long-term liabilities. Decisions will be based on the outcome of financial option appraisals and best value considerations. Any movement between these separate limits will be reported to the next Council meeting.

	2019/20 Actual £'000	2020/21 Original Estimate £'000	2020/21 Actual £'000
Borrowing	79,500	120,000	98,000
Other Long-term Liabilities	51	15	20
Total	79,551	120,015	98,020

For information the 2021/22 operational boundary has been set at £135m and the authorised limit £165m. This was approved by full Council in February 2021 as part of the Annual Capital, Investment and Treasury Management Strategy report.

Compliance

52. The Council operated within all of the Prudential Indicators during 2020/21.

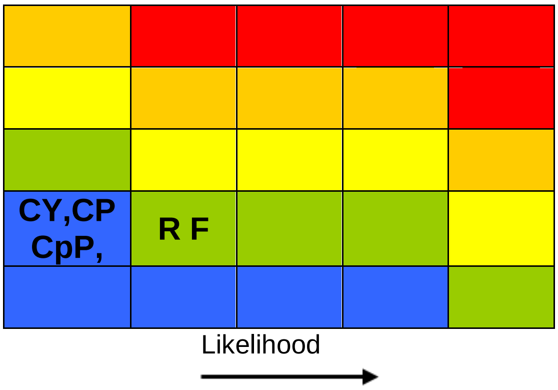
Financial Implications

53. There are no additional financial implications in reviewing the attached Treasury Management Strategy.

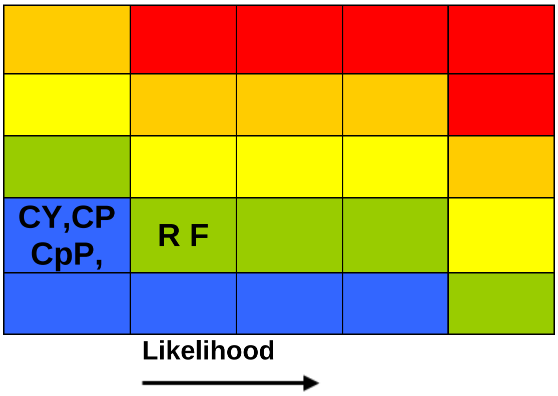
South Somerset District Council

Risk Matrix

Risk Profile before officer recommendations



Risk Profile after officer recommendations



Key

Categories	**Colours** (for further detail please refer to Risk management strategy)
R - Reputation	High impact and high probability
CpP - Corporate Plan Priorities	Major impact and major probability
CP - Community Priorities	Moderate impact and moderate probability
CY - Capacity	Minor impact and minor probability
F - Financial	Insignificant impact and insignificant probability

Council Plan Implications

54. The performance of the Council's investment portfolio and the associated investment and borrowing strategies are closely linked to the Council Plan. The funds invested and those that are externally borrowed exposes the Council to financial risks. The approved strategies ensure the risks are identified, monitored and controlled therefore ensuring the investments are secure whilst maximising the return on investments.

55. The return on investments, and ensuring borrowing costs are minimised, is a key element of the Medium Term Financial Plan which is aligned to the Council Plan and contributes to enabling the delivery of the Council's priorities for the local community.

Carbon Emissions and Climate Change Implications

56. There are no implications in approving this report.

Equality and Diversity Implications

57. There are no implications in approving this report.

Privacy Impact Assessment

South Somerset District Council

58. There is no personal information included in this report.

Background Papers

59. Treasury Management Strategy 2020/21 (Full Council February 2020)
Prudential Indicators and MRP Statement 2020/21
Capital Outturn 2020/21

APPENDIX A – Additional commentary from Arlingclose

External Context

Economic background: The coronavirus pandemic dominated 2020/21, leading to almost the entire planet being in some form of lockdown during the year. The start of the financial year saw many central banks cutting interest rates as lockdowns caused economic activity to grind to a halt. The Bank of England cut Bank Rate to 0.1% and the UK government provided a range of fiscal stimulus measures, the size of which has not been seen in peacetime.

Some good news came in December 2020 as two COVID-19 vaccines were given approval by the UK Medicines and Healthcare Products Regulatory Agency (MHRA). The UK vaccine rollout started in earnest; over 31 million people had received their first dose by 31st March.

A Brexit trade deal was agreed with only days to spare before the 11pm 31st December 2020 deadline having been agreed with the European Union on Christmas Eve.

The Bank of England (BoE) held Bank Rate at 0.1% throughout the year but extended its Quantitative Easing programme by £150 billion to £895 billion at its November 2020 meeting. In its March 2021 interest rate announcement, the BoE noted that while GDP would remain low in the near-term due to COVID-19 lockdown restrictions, the easing of these measures means growth is expected to recover strongly later in the year. Inflation is forecast to increase in the near-term and while the economic outlook has improved there are downside risks to the forecast, including from unemployment which is still predicted to rise when the furlough scheme is eventually withdrawn.

Government initiatives supported the economy and the Chancellor announced in the 2021 Budget a further extension to the furlough (Coronavirus Job Retention) scheme until September 2021. Access to support grants was also widened, enabling more self-employed people to be eligible for government help. Since March 2020, the government schemes have help protect more than 11 million jobs.

Despite the furlough scheme, unemployment still rose. Labour market data showed that in the three months to January 2021 the unemployment rate was 5.0%, in contrast to 3.9% recorded for the same period 12 months ago. Wages rose 4.8% for total pay in nominal terms (4.2% for regular pay) and was up 3.9% in real terms (3.4% for regular pay). Unemployment is still expected to increase once the various government job support schemes come to an end.

Inflation has remained low over the 12-month period. Latest figures showed the annual headline rate of UK Consumer Price Inflation (CPI) fell to 0.4% year/year in February, below expectations (0.8%) and still well below the Bank of England's 2% target. The ONS' preferred measure of CPIH which includes owner-occupied housing was 0.7% year/year (1.0% expected).

After contracting sharply in Q2 (Apr-Jun) 2020 by 19.8% q/q, growth in Q3 and Q4 bounced back by 15.5% and 1.3% respectively. The easing of some lockdown measures in the last quarter of the calendar year enabled construction output to continue, albeit at a much slower pace than the 41.7% rise in the prior quarter. When released, figures for Q1 (Jan-Mar) 2021 are expected to show a decline given the national lockdown.

After collapsing at an annualised rate of 31.4% in Q2, the US economy rebounded by 33.4% in Q3 and then a further 4.1% in Q4. The US recovery has been fuelled by three major pandemic relief stimulus packages totalling over $5 trillion. The Federal Reserve cut its main interest rate to between 0% and 0.25% in March 2020 in response to the pandemic and it has remained at the same level since. Joe Biden became the 46th US president after defeating Donald Trump.

The European Central Bank maintained its base rate at 0% and deposit rate at -0.5% but in December 2020 increased the size of its asset purchase scheme to €1.85 trillion and extended it until March 2022.

Financial markets: Monetary and fiscal stimulus helped provide support for equity markets which rose over the period, with the Dow Jones beating its pre-crisis peak on the back of outperformance by a small number of technology stocks. The FTSE indices performed reasonably well during the period April to November, before being buoyed in December by both the vaccine approval and Brexit deal, which helped give a boost to both the more internationally focused FTSE 100 and the more UK-focused FTSE 250, however they remain lower than their pre-pandemic levels.

Ultra-low interest rates prevailed throughout most of the period, with yields generally falling between April and December 2020. From early in 2021 the improved economic outlook due to the new various stimulus packages (particularly in the US), together with the approval and successful rollout of vaccines, caused government bonds to sell off sharply on the back of expected higher inflation and increased uncertainty, pushing yields higher more quickly than had been anticipated.

The 5-year UK benchmark gilt yield began the financial year at 0.18% before declining to -0.03% at the end of 2020 and then rising strongly to 0.39% by the end of the financial year. Over the same period the 10-year gilt yield fell from 0.31% to 0.19% before rising to 0.84%. The 20-year declined slightly from 0.70% to 0.68% before increasing to 1.36%.

1-month, 3-month and 12-month SONIA bid rates averaged 0.01%, 0.10% and 0.23% respectively over the financial year.

The yield on 2-year US treasuries was 0.16% at the end of the period, up from 0.12% at the beginning of January but down from 0.21% at the start of the financial year. For 10-year treasuries the end of period yield was 1.75%, up from both the beginning of 2021 (0.91%) and the start of the financial year (0.58%).

German bund yields continue to remain negative across most maturities.

Credit review: After spiking in March 2020, credit default swap spreads declined over the remaining period of the year to broadly pre-pandemic levels. The gap in spreads between UK ringfenced and non-ringfenced entities remained, albeit Santander UK is still an outlier compared to the other ringfenced/retail banks. At the end of the period Santander UK was trading the highest at 57bps and Standard Chartered the lowest at 32bps. The other ringfenced banks were trading around 33 and 34bps while Nationwide Building Society was 43bps.

Credit rating actions to the period ending September 2020 have been covered in previous outturn reports. Subsequent credit developments include Moody's downgrading the UK sovereign rating to Aa3 with a stable outlook which then impacted a number of other UK institutions, banks and local government. In the last quarter of the financial year S&P upgraded Clydesdale Bank to A- and revised Barclay's outlook to stable (from negative) while Moody's downgraded HSBC's Baseline Credit Assessment to baa3 whilst affirming the long-term rating at A1.

The vaccine approval and subsequent rollout programme are both credit positive for the financial services sector in general, but there remains much uncertainty around the extent of the losses banks and building societies will suffer due to the economic slowdown which has resulted due to pandemic-related lockdowns and restrictions. The institutions and durations on the Authority's counterparty list recommended by treasury management advisors Arlingclose remain under constant review, but at the end of the period no changes had been made to the names on the list or the recommended maximum duration of 35 days.

South Somerset District Council

Risk Update

Director:	Nicola Hix, Director Support Services & Strategy
Lead Specialist:	Brendan Downes, People Performance & Change Lead
Contact Details:	Brendan.downes@southsomerset.gov.uk

Purpose of the Report

This report is provided to inform committee of the status of the Consolidated Risk Register (Strategic and Category Risks) as at 1st April 2021, as well as to provide and update on risk management arrangements across the authority.

Public Interest

Risk can be described as "The effect of uncertainty on objectives, often described by an event or a change in circumstances"

Risk Management can be described as the coordinated activities to direct and control an organisation with regard to risk.

South Somerset District Council look to ensure effective risk management arrangements are in place to help the Council maximises its opportunities and minimises the impact of the risks it faces. Effective risk management should improve our ability to deliver key priorities, improve outcomes for residents, maintain good governance and minimise any damage to its reputation

Recommendations

That Audit Committee notes:

1. The risk management arrangements in place and provides comment.
2. The status of the risk registers at 1st April 2021 as summarised in Appendix 1.

Background

The risk approach within SSDC is based on the organisational ethos of "One Team". This is intended to create a risk management approach that looks at risk holistically across the organisation, rather than focussing on performance risks in individual functional units which can lead to silo thinking and inefficiencies.

The SSDC risk approach is now based on a framework of risk registers, which can be summarised as:

- Strategic Risk register which records the significant long term risks facing the authority
- Category registers which will capture corporate risks as well as provide oversight of all project risks coded to a specific category
- "Project" risk registers, developed for projects, initiatives and significant areas of work

The principles of how risks are managed in the authority are described in the risk management policy issued February 2020

Report Detail

A summary of risk position at 31st March 2021 and points of note are:

1. The previously agreed approach to maintain and update the risk register through review with risk category leads and by utilizing established forums such as the Health & Safety Steering Group and People Managers Forum has been challenging to maintain. Under normal circumstances most of these groups meet at least quarterly to review risks formally, however COVID-19 as well as SSDC's direct involvement in the rollout of the vaccination programme has impacted both on "business as usual" activities as well as the availability of officers. It is hoped that most forums are now able to meet regularly again and more regular reviews of risks will be re-established.

2. Furthermore the last few months have seen a number of significant changes in membership of the senior leadership team and across LMT, a situation which is ongoing. As well as impacting on availability of key personnel this has required reassignment of a significant number of risks and work is ongoing to confirm new risk owners as appointments are made.

3. In this context, the 2020 Q4 risk position update should be considered "partial" as a number of risks have not been formally reviewed within the period. A summary showing the date of last update of individual risks as well as changes in the risk profile compared to the previous quarter are shown in Appendix 1, "2020.Q4 Risk Movements ranked by residual risk score".

4. **Key points to note with regards to content**: The consolidated risk register includes the strategic and category risk registers as developed for:
    - Finance
    - Staffing and capacity
    - Health and safety
    - Reputation
    - Project and programme delivery
    - Delivery of services
    - Governance and legal

5. Finance Risks: A specific review on financial risks will be held with the newly appointed Section 151 and Lead Specialist – Finance following conclusion of year end activities. Date TBC.

6. Staffing and capacity: Staffing and Wellbeing dashboards are now established and reviewed on a monthly through the People Managers Forum. A specific risk review is scheduled for the 8th June with the group which will be captured in the 2021/22 Quarter 1 register.

7. Health and safety Risks: The recent 'critical friend' H&S maturity assessment conducted by Zurich concluded that SSDC demonstrated a commitment to developing a practical and effective approach to health and safety management. However, the assessment recommended risk improvement actions relating to the a number of areas including Competent person(s), planning and policy, safe systems/permits to work as well as Monitoring and audit. In that context the H&S risks will be updated and actions from the improvement plan will be recorded in the risk register as they are agreed.

8. Reputational Risk: No update

9. Project and programme delivery: No Updates. (n.b. Project risk registers related to the regeneration projects are not included in this consolidated risk register as they have their own project boards and governance structure where these project risks are reviewed).

10. Delivery of services: It is clear that challenges from the effects of the pandemic on our residents and businesses are emerging, and the impact on service delivery will require ongoing review. A wider review of the risks for this area will be scheduled with the new Directors for Service Delivery and Place and Recovery. Digital Risks are seen to be reducing as many elements of the Digital Strategy have been successfully implemented, and benefits are being realised.

11. Governance and legal Risks: A new Monitoring Officer and new Section 151 were appointed in Q4. A thorough review of Governance and Legal risks will be scheduled when these officers have had the opportunity to review and appraise current arrangements.

12. COVID 19 risk register: The risk register for COVID 19 was introduced in response to the pandemic and is reviewed and updated by GOLD. It is anticipated that the COVID risk register may be integrated to the corporate risk structure in the coming months as we return to some normality.

13. **Audit findings.** It should be noted a SWAP Risk audit was conducted in April 21, with the provisional report expected end of May. A summary of the audit findings will be shared with Audit committee on the next committee meeting scheduled for July 29th 2021.

Financial Implications

There are no direct financial implications as a result of this report.

Council Plan Implications

Aligned to our Council Plan values of empowering a confident, flexible workforce

Carbon Emissions and Climate Change Implications

None.

Equality and Diversity Implications

None.

Background Papers

None.

Risk Summary, to provide an overview of the content of the strategic and category risk registers and quarterly changes in the SSDC risk profile as recorded in full risk regist By Risk Category **31.March.2021**

Ref	Risk Title	Category	Owner	Last Updated	@ 30/01/2021 Inherent Rating 2020.Q3	@ 30/01/2021 Residual Rating 2020.Q3	@ 31/03/2021 Inherent Rating 2020.Q4	@ 31/03/2021 Residual Rating 2020.Q4	Movement Inherent Rating Change	Movement Residual Rating Change	Status	Summary
COV 08	Drain on Financial reserves due to COVID (See also F07)	Financial	Jo Nacey	14/12/20	25	23	25	23	0	0	Open	
HS02	Incident, accident or injury in Public spaces that SSDC Manage	Health & Safety	Katy Menday	31/03/21	20	14	24	23	4	9	Open	Risk impact re-scored at 5 in line with SWAP recommendation
HS01	Threats to Staff from verbal or physical attack	Health & Safety	Helen Morris	31/03/21	19	18	23	22	4	4	Open	Risk impact re-scored at 5 in line with SWAP recommendation
HS03	Incident, accident or injury in SSDC Premises (SSDC Occupied & unmanne	Health & Safety	R Orrett.	31/03/21	14	13	23	22	9	9	Open	Risk impact re-scored at 5 in line with SWAP recommendation
HS05	Employee or public harm from exposure to hazardous materials	Health & Safety	Vicki Dawson	31/03/21	19	18	23	22	4	4	Open	Risk impact re-scored at 5 in line with SWAP recommendation
HS06	Accidents when conducting Operation and maintenance	Health & Safety	Chris Cooper	31/03/21	19	18	23	22	4	4	Open	Risk impact re-scored at 5 in line with SWAP recommendation
COV 05	Economic Infrastructure slowdown /collapse impacting regeneration & ca	Project or programme d	Martin Woods	04/01/21	20	20	20	20	0	0	Open	
COV 20	Increasing numbers of public needing our services	Delivery of Services	Netta Meadows/Kirsty L	04/01/21	21	20	21	20	0	0	Open	
COV 03	Lack of clear "messaging" around COVID from SSDC	Reputation	Alex Parmley	16/09/20	20	19	20	19			Open	Update Overdue
F07	Pressure on reserves	Financial	S151	22/12/20	24	19	24	19	0	0	Open	Risk reduced but not enough to change rating.
PP02	Poor execution of Projects	Project or programme d	Brendan Downes	30/12/20	20	19	20	19	0	0	Open	
ST07	**STRATEGIC: Civil emergencies and Business continuity disruptions**	Delivery of Services	Kirsty Larkins	01/12/20	19	19	19	19	0	0	Open	
D01	The Digital Strategy is not fully implemented	Delivery of Services	Toffer Beattie	31/03/21	19	19	19	18	0	-1	Open	residual likelihood is lowered
D02	The Digital Strategy fails to deliver outcomes and benefits	Delivery of Services	Toffer Beattie	31/03/21	19	19	19	18	0	-1	Open	residual likelihood is lowered
GL07	High profile member decisions against officer recommendation	Governance & Legal	Monitoring Officer / Lea	15/10/20	19	18	19	18			Open	To be reviewed with New Section 151 & Monitoring Officer
PP01	Initiation of projects that are either unviable or not worthwhile	Project or programme d	Brendan Downes	30/12/20	19	18	19	18	0	0	Open	Actions updated
FS06	Members portal does not provide capability that was promised	Reputation	Steph Gold	14/12/20	16	16	16	16	0	0	Open	
ST03/GL01	**STRATEGIC: Significant change in government legislation**	Governance & Legal	Monitoring Officer / Lea	14/12/20	21	16	21	16	0	0	Open	
COV 04	Negative resident perceptions of SSDC delivery / response during COVID	Reputation	Richard Birch	02/10/20	20	15	20	15			Open	Update Overdue
COV 07	Strategic: Lapse / failure of commissioned services	Delivery of Services	Senior Leadership Team	16/09/20	20	15	20	15			Open	Update Overdue
PP03	Lack of organisational knowledge base on projects	Project or programme d	Brendan Downes	30/12/20	14	14	15	15	1	1	Open	Likelihood increased
SC02	Deterioration in quality of work being delivered	Staffing / Capacity	Brendan Downes / PMF	30/12/20	20	14	20	15	0	1	Open	Likelihood increased due to ongoing work pressures. PMF Review sche
COV 02	Mid/long-term burnout of employees due to stress / anxiety / depressior	Staffing / Capacity	Nicky Hix (Lead) with Jer	15/12/20	20	14	20	14	0	0	Open	
COV 12	No / ineffective Safe Systems of Work for Evacuation of people/commun	Health & Safety	Kirsty Larkins	01/12/20	19	14	19	14	0	0	Open	Actions updated
F02	Overspends of budgets / Under achievement of income	Financial	S151	22/12/20	20	14	20	14	0	0	Open	
ST04/ SC01	**STRATEGIC: Falling staff retention**	Staffing / Capacity	Jenny Clayton / PMF	31/12/20	20	14	20	14	0	0	Open	PMF Review scheduled 8/6/21
COV 01	Ongoing Impact on staffing levels and key roles due to the pandemic (Illn	Staffing / Capacity	Nicky Hix (Lead) with Jer	15/12/20	19	13	19	13	0	0	Open	
COV 13	Services are unable to operate safely due to shortage of PPE	Delivery of Services	Kirsty Larkins H&S Exec	01/12/20	14	13	14	13	0	0	Open	
COV 17	Increased risk of challenge to decision making processes and outcomes	Governance & Legal	Monitoring Officer / Lea	21/07/20	16	13	16	13			Open	Update Overdue
F03	Missed Funding / income	Financial	S151 / Specialist Team M	04/01/21	24	13	24	13	0	0	Open	
F06	Impact on borrowings & Investments / Challenges or inability to secure c	Financial	S151	22/12/20	24	13	24	13	0	0	Open	
GL02	Officer Inducement	Governance & Legal	Monitoring Officer / Lea	15/10/20	23	13	23	13			Open	To be reviewed with New Section 151 & Monitoring Officer
GL03	Data and information breaches or losses.	Governance & Legal	Brendan Downes	30/12/20	23	13	23	13	0	0	Open	To be reviewed with New Section 151 & Monitoring Officer
GL06	Statutory duties not being carried out	Governance & Legal	Netta Meadows	09/10/20	19	13	19	13			Open	To be reviewed with New Section 151 & Monitoring Officer
F04	Challenge to integrity of the financial system	Financial	S151	22/12/20	19	12	19	12	0	0	Open	
ST01/F01	**STRATEGIC: Inability of the council to achieve a balanced budget**	Financial	S151 / SLT	15/12/20	19	12	19	12	0	0	Open	
SC03	Inadequate insight to current and future work requirements	Staffing / Capacity	Brendan Downes / PMF	30/12/20	16	11	16	11	0	0	Open	Ongoing uncertainty of LGR in Somerset and pandemic effects. PMF Re
COV 09	Retention and resilience of redeployed staff	Staffing / Capacity	Kirsty Larkins / PMF	01/12/20	14	9	14	9	0	0	Open	
COV 10	Volume of redeployment/recruitment demand	Staffing / Capacity	Kirsty Larkins	01/12/20	14	9	14	9	0	0	Open	
COV 11	Technology infrastructure no longer able to support business	Delivery of Services	Toffer Beattie	27/11/20	14	9	14	9	0	0	Open	
GL05	Failure to comply with corporate procedures	Governance & Legal	Kirsty Larkins	01/12/20	15	9	15	9	0	0	Open	To be reviewed with New Section 151 & Monitoring Officer
COV 15	Negative Business perception of SSDC due to Rate relief and business gra	Reputation	Netta Meadows	04/01/21	14	8	14	8	0	0	Open	
COV 19	Reduced "real-time" organisational Intelligence gathering about South Sc	Delivery of Services	Kirsty Larkins	01/12/20	13	8	13	8	0	0	Open	
COV21	Negative resident perception due to insufficient roll out of Isolation	Delivery of Services	Netta Meadows/Kirsty L	04/01/21	15	8	15	8	0	0	Open	
F05	Fraudulent actions affecting Finance systems	Financial	S151 / Monitoring Office	22/12/20	14	6	14	6	0	0	Open	
F08	Ineffective partnerships failing to provide added value	Financial	TBC	15/10/20	13	6	13	6			Open	Update Overdue. ownership to be clarified
COV 14	Strain on SSDC vehicle pool	Delivery of Services	Clare Pestell (Chris Coop	21/09/20	9	3	9	3			Open	Update Overdue
COV 18	Risks to Staff Professional and personal Development	Staffing / Capacity	Kirsty Larkins	01/12/20	13	2	13	2	0	0	Open	
GL04	Theft, loss or misuse of council assets	Governance & Legal	S151	04/01/21	14	2	14	2	0	0	Open	To be reviewed with New Section 151 & Monitoring Officer

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Report Title: Review of the Audit Committee's Terms of Reference

Strategic Director:	Nicola Hix, Director Support Services & Strategy
Lead Officer:	Karen Watling, Interim S151 Officer
Contact Details:	Karen.Watling@southsomerset.gov.uk

Purpose of the Report

To obtain Audit Committee's approval to establish a working group to review the committee's Terms of Reference (ToRs).

Public Interest

Audit committees are a key component of corporate governance and an important source of assurance about an organisation's arrangements for managing risk, maintaining an effective control environment, and reporting on financial and other performance.

It is good practice to periodically review the remit and working practices of the Audit Committee to ensure they are in line with any updated national guidance and/or legislative changes and therefore remaining fit for purpose.

This report recommends that a joint Member/Officer working group is established to review the Audit Committee's existing Terms of Reference (ToRs) to see if any improvements or changes need to be made in line with the guidance contained in the CIPFA (Chartered Institute of Public Finance and Accountancy) publication entitled "*Audit Committees; Practical Guidance for Local Authorities and Police*" (2018 edition).

The working group will also review any changes that may be needed arising from MHCLG's (Ministry of Housing, Communities & Local Government) response to Sir Tony Redmond's "*Independent review into the oversight of local audit and the transparency of local authority financial reporting*" (September 2020).

Any recommendations for changes to the ToRs would come to a future Audit Committee for review and then on to full Council for approval.

Recommendations

1. That a working group comprising of representative Members of the Audit Committee and relevant officers is established to review the committee's Terms of Reference.
2. That the membership of the working group, and the scope of its review, is agreed as per the details set out in this report.

3. That the working group reports back into the Audit Committee ideally at its next meeting, (subject to other work load), for it to review any proposals prior to them being sent to full Council for approval.

Background

SSDC's Constitution (Part 2, Article 8) sets out the Audit Committee's current Terms of Reference as follows:

Scope of Audit Committee: The Council shall appoint an Audit Committee which provides independent assurance of the adequacy of the risk management framework and the associated control environment (ranging from standing orders, financial procedures etc.), independent scrutiny of the authority's financial and non-financial performance, to the extent that it affects the authority's exposure to risk and weakens the control environment and it oversees the financial reporting process.

The Audit Committee shall:

- Approve the Strategic and Annual Internal Audit Plans.
- Receive summaries of Internal Audit reports and seek assurance from management that action has been taken.
- Consider the reports of external audit and inspection agencies and seek assurance from management that action has been taken.
- Consider the effectiveness of SSDC's risk management arrangements, the control environment and associated anti-fraud and corruption arrangements and seek assurance from management that action is being taken.
- Review the annual Statement of Internal Control and monitor associated action plans.
- Review the SSDC's Code of Corporate Governance and ensure it is kept up to date and reflects best practice. This will include regular reviews of the Council's Constitution and an overview of the risk management.
- Receive reports from management on the promotion of good corporate governance.
- Review and approve the annual Statement of Accounts, external auditor's opinion and reports to members and monitor management action in response to issues raised.

Review of the Audit Committee's ToRs

As stated above, it is good practice to periodically review the remit and responsibilities (known as "Terms of Reference") to ensure they remain in line with good practice and are fit for purpose.

CIPFA's (Chartered Institute of Public Finance and Accountancy) publication entitled "*Audit Committees; Practical Guidance for Local Authorities and Police*" (2018 edition) is acknowledged as the primary guidance in this area of activity. The 2018 edition, which is the most recent edition, offers a comprehensive package of guidance

South Somerset District Council

including updates from other CIPFA publications such as the "*Public Sector Internal Audit Standards*" (2017), "*Delivering Good Governance in Local Government:*

Framework" (2016) and the "*Code of Practice on Managing the Risk of Fraud and Corruption"* (2014).

The working group will review the Audit Committee's ToRs to see if any improvements or changes need to be made in line with the guidance contained within the CIPFA publication.

In addition, the working group will also review any changes that may be needed arising from MHCLG's (Ministry of Housing, Communities & Local Government) response to Sir Tony Redmond's "*Independent review into the oversight of local audit and the transparency of local authority financial reporting*" (September 2020).

MHCLG asked Sir Tony Redmond in July 2019 to undertake an independent review into the arrangements in place to support the transparency and quality of local authority financial reporting and external audit in England. MHCLG published its response to the review in September 2020 which included, amongst other matters, proposals to change the current date for the publication of audited local authority accounts, reviewing the governance arrangements within local authorities (for example requiring that an annual report is submitted to Full Council by the external auditor), and preparing a new statement to the accounts called a standardised statement of service costs. These proposals may require a change to the Audit Committee's ToRs.

It is proposed that the Member/Officer working group is comprised of: The Chair and Vice-Chair of the Audit Committee, two (or three) volunteer members of the Audit Committee, the S151 and Deputy S151 Officers, the Monitoring Officer, and the Assistant Director of SWAP (Internal Audit Services).

It is further proposed that the working group reports back into the Audit Committee ideally at its next meeting, (subject to other work load), for it to review any proposals prior to them being sent to full Council for approval.

Financial Implications

There are no financial implications arising from agreeing this report. The review being proposed can be undertaken within the current agreed budget.

Council Plan Implications

The proposals in this report contribute to SSDC's vison of being open and transparent and actively communicating, engaging and listening to feedback.

Carbon Emissions and Climate Change Implications

There are no implications arising from agreeing this report.

Equality and Diversity Implications

There are no implications arising from agreeing this report.

South Somerset District Council

Background Papers

- CIPFA (Chartered Institute of Public Finance and Accountancy) "*Audit Committees; Practical Guidance for Local Authorities and Police*" (2018 edition).
- MHCLG's "*Local authority financial reporting and external audit: government response to the Redmond review*" (December 2020)

South Somerset District Council

Audit Committee Forward Plan

Director:	Nicola Hix, Strategy and Support Services
Lead Officer:	Michelle Mainwaring, Case Officer (Strategy & Commissioning)
Contact Details:	michelle.mainwaring@southsomerset.gov.uk

Purpose of the Report

This report informs Members of the agreed Audit Committee Forward Plan.

Recommendations

Members are asked to note and comment upon the proposed Audit Committee Forward Plan as attached.

Area East Committee Forward Plan

The forward plan sets out items and issues to be discussed over the coming few months and is reviewed annually.

Items marked *in italics* are not yet confirmed.

Background Papers

None.

South Somerset District Council

Audit Committee Forward Plan

Meeting Date	Item	Responsible Officer
29th July 21	Internal Audit Plan Progress Report 2021/22 – Q1	Alastair Woodland, Assistant Director (SWAP)
	Redmond Review Consultation	S151 Officer
September 21 Date to be confirmed	Annual Governance Statement	S151 Officer
	External Audit – Audit Findings Report	Beth Garner - Manager (Grant Thornton)
	Approve Annual Statement of Accounts	Lead Specialist – Finance (Deputy S151 Officer) / S151 Officer
October 21 Date to be confirmed	Internal Audit Plan Progress Report 2021/22 – Q2	Alastair Woodland, Assistant Director (SWAP)
	Treasury Management Practices	Lead Specialist – Finance (Deputy S151 Officer)
	Treasury Management Mid-Year Performance and Strategy Update (to go on to Council)	Lead Specialist – Finance (Deputy S151 Officer)
	External Audit – Annual Audit Letter	Beth Garner - Manager (Grant Thornton)
TBC	*Appointment of Powys County Council to undertake Fraud Investigation Work*	*S151 Officer*
	Annual Fraud Programme Update	*TBC*
	Monitoring the recommendations of SWAP following audits.	*Alastair Woodland, Assistant Director (SWAP)*