Public Document Pack

Hampshire County Council

NOTICE OF MEETING

Meeting	Audit Committee
Date and Time	Thursday, 21st February, 2019 at 2.00 pm
Place	Chute Room, EII South, The Castle, Winchester
Enquiries to	members.services@hants.gov.uk

John Coughlan CBE
Chief Executive
The Castle, Winchester SO23 8UJ

FILMING AND BROADCAST NOTIFICATION
This meeting may be recorded and broadcast live on the County Council's website. The meeting may also be recorded and broadcast by the press and members of the public – please see the Filming Protocol available on the County Council's website.

AGENDA

1. APOLOGIES FOR ABSENCE

To receive any apologies for absence.

2. DECLARATIONS OF INTEREST

All Members who believe they have a Disclosable Pecuniary Interest in any matter to be considered at the meeting must declare that interest and, having regard to the circumstances described in Part 3 Paragraph 1.5 of the County Council's Members' Code of Conduct, leave the meeting while the matter is discussed, save for exercising any right to speak in accordance with Paragraph 1.6 of the Code. Furthermore all Members with a Non-Pecuniary interest in a matter being considered at the meeting should consider whether such interest should be declared, and having regard to Part 5, Paragraph 2 of the Code, consider whether it is appropriate to leave the meeting while the matter is discussed, save for exercising any right to speak in accordance with the Code.

3. MINUTES OF PREVIOUS MEETING HELD ON 20 DECEMBER 2018 (Pages 5 - 8)

To confirm the minutes of the previous meeting.

4. DEPUTATIONS

To receive any deputations notified under Standing Order 12.

5. CHAIRMAN'S ANNOUNCEMENTS

To receive any announcements the Chairman may wish to make.

6. INFORMATION COMPLIANCE - USE OF REGULATED INVESTIGATORY POWERS (Pages 9 - 14)

To receive the quarterly update on the County Council's use of regulated investigatory powers.

7. TREASURY MANAGEMENT STRATEGY STATEMENT 2019/20 TO 2020/21 (Pages 15 - 36)

To receive the report of the Director of Corporate Resources – Corporate Services with an update on the treasury management strategy.

8. HAMPSHIRE COUNTY COUNCIL AUDIT PLANNING REPORT 2018/19 (Pages 37 - 76)

To receive the external audit planning report for Hampshire County Council from the for 2018/19.

9. HAMPSHIRE PENSION FUND AUDIT PLANNING REPORT 2018/19 (Pages 77 - 114)

To receive the external audit planning report for the Hampshire Pension Fund for 2018/19.

10. MINUTES OF THE HAMPSHIRE PENSION FUND PANEL AND BOARD MEETING - 15 NOVEMBER 2018 (LESS EXEMPT) (Pages 115 - 122)

To receive the non-exempt minutes of the Hampshire Pension Fund Panel and Board meeting held on 15 November 2018.

11. EXCLUSION OF THE PRESS AND PUBLIC

To resolve that the public be excluded from the meeting during the following item of business, as it is likely, in view of the nature of the business to be transacted or the nature of the proceedings, that if members of the public were present during this item there would be disclosure to them of exempt information within Paragraphs 3 of Part 1 of Schedule 12A to the Local Government Act 1972, and further that in all the circumstances of the cases, the public interest in maintaining the exemption outweighs the public interest in disclosing the information, for the reasons set out in the exempt minutes.

12. MINUTES OF THE HAMPSHIRE PENSION FUND PANEL AND BOARD MEETING - 15 NOVEMBER 2018 (EXEMPT) (Pages 123 - 128)

To receive the exempt minutes of the Hampshire Pension Fund Panel and Board meeting held on 15 November 2018.

ABOUT THIS AGENDA:

On request, this agenda can be provided in alternative versions (such as large print, Braille or audio) and in alternative languages.

ABOUT THIS MEETING:

The press and public are welcome to attend the public sessions of the meeting. If you have any particular requirements, for example if you require wheelchair access, please contact members.services@hants.gov.uk for assistance.

County Councillors attending as appointed members of this Committee or by virtue of Standing Order 18.5; or with the concurrence of the Chairman in connection with their duties as members of the Council or as a local County Councillor qualify for travelling expenses.

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AT A MEETING of the Audit Committee of HAMPSHIRE COUNTY COUNCIL held at The Castle, Winchester on Thursday, 20th December, 2018:

Chairman:
p. Councillor Keith Evans

p. Councillor Alexis McEvoy
a. Councillor Dominic Hiscock
p. Councillor Keith House
p. Councillor Mark Kemp-Gee
p. Councillor Derek Mellor
p. Councillor Rob Mocatta
p. Councillor Lance Quantrill
p. Councillor Tom Thacker

84. **APOLOGIES FOR ABSENCE**

Apologies were received from Councillor Hiscock.

85. **DECLARATIONS OF INTEREST**

Members were mindful that where they believed they had a Disclosable Pecuniary Interest in any matter considered at the meeting they must declare that interest at the time of the relevant debate and, having regard to the circumstances described in Part 3, Paragraph 1.5 of the County Council's Members' Code of Conduct, leave the meeting while the matter was discussed, save for exercising any right to speak in accordance with Paragraph 1.6 of the Code. Furthermore Members were mindful that where they believed they had a Non-Pecuniary interest in a matter being considered at the meeting they considered whether such interest should be declared, and having regard to Part 5, Paragraph 2 of the Code, considered whether it was appropriate to leave the meeting whilst the matter was discussed, save for exercising any right to speak in accordance with the Code.

86. **MINUTES OF PREVIOUS MEETING - 26 JULY 2018**

The minutes of the meeting held on 26 July 2018 were agreed as a correct record and signed by the Chairman.

87. **DEPUTATIONS**

There were no deputations.

88. **CHAIRMAN'S ANNOUNCEMENTS**

There were no announcements.

89. **INFORMATION COMPLIANCE - USE OF REGULATED INVESTIGATORY POWERS**

The Committee considered the report of the Director of Transformation and Governance– Corporate Services regarding the County Council's use of regulated investigatory powers.

RESOLVED:

That the Audit Committee receives and notes the data regarding the County Council's use of surveillance powers as attached at Appendix 1 to the report.

90. **INTERNAL AUDIT PROGRESS REPORT (NOVEMBER 2018)**

The Committee considered the report of the Deputy Chief Executive and Director of Corporate Resources with the internal audit progress report.

In response to Members' questions, it was confirmed that:

- The customer feedback, referred to on page 25 of the agenda pack, had been obtained via survey. The survey had been sent to Audit Committee members, Chief Officers and key contacts from all organisations who were included within the Southern Internal Audit Partnership.
- The overdue management actions, referred to on page 26 of the agenda pack, were being addressed with a thorough action plan. Lead officers with the responsibility for each entry had provided estimated timescales for completion of required actions and Internal Audit intended to follow up with the lead officers until the required action was carried out.

RESOLVED:

That the Audit Committee notes the Internal Audit Progress report for the period to November 2018 as attached at Appendix 1 to the report.

91. **TREASURY MANAGEMENT MONITORING REPORT 2018/19**

The Committee considered the report of the Deputy Chief Executive and Director of Corporate Resources with the treasury management mid year monitoring report.

In response to Members' questions, it was confirmed that investment opportunities were always carefully selected in liaison with the County Council's independent advisors and reviewed by the Director. The Committee noted that a further update on any return from investments would be provided at a future meeting. Members also queried why, given the attractive percentage returns, it was taking so long to commit to the agreed £200m investment level. The Committee were assured that this was being progressed and there will be increased level of investment going forward.

RESOLVED:

That the Audit Committee notes that the mid-year report on treasury management and also notes that this has been reported to both Cabinet and Full Council.

92. **ANNUAL AUDIT LETTER - 2017/18**

In relation to this item, Councillor House declared a non-pecuniary interest as a Board member of the Public Sector Audit Appointments (PSAA) who appoint Ernst and Young as a principal body audit firm.

The Committee received and noted the annual audit letter for 2017/18 from the external auditors, Ernst and Young, following the completion of the audit procedures for the year.

93. **MINUTES OF THE HAMPSHIRE PENSION FUND PANEL AND BOARD MEETING - 22 JUNE, 27 JULY AND 28 SEPTEMBER 2018 (LESS EXEMPT)**

The Committee received and noted the non-exempt minutes of the Hampshire Pension Fund and Board meeting held on 22 June, 27 July and 28 September 2018.

94. **EXCLUSION OF THE PRESS AND PUBLIC**

It was resolved that any press and public who had been present were excluded from the meeting during the following items of business, as it was likely, in view of the nature of the business to be transacted or the nature of the proceedings, that if members of the public were present during these items there would have been disclosure to them of exempt information within Paragraph 3 of Part I Schedule 12A to the Local Government Act 1972, and further that in all the circumstances of the case, the public interest in maintaining the exemption outweighed the public interest in disclosing the information, for the reasons set out in the minutes.

95. **MINUTES OF THE HAMPSHIRE PENSION FUND PANEL AND BOARD MEETING - 22 JUNE, 27 JULY AND 28 SEPTEMBER 2018 (EXEMPT)**

The Committee received and noted the exempt minutes of the Hampshire Pension Fund and Board meeting held on 22 June, 27 July and 28 September 2018.

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HAMPSHIRE COUNTY COUNCIL

Report

Committee/Panel:	Audit Committee
Date:	21 February 2019
Title:	Information Compliance – Use of Regulated Investigatory Powers
Report From:	Director of Transformation and Governance – Corporate Services

Contact name: Peter Andrews

Tel: 01962 847309 **Email:** peter.andrews@hants.gov.uk

1. Recommendation

1.1 That the Audit Committee receives and notes the data regarding the County Council's use of surveillance powers as attached at Appendix 1.

CORPORATE OR LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	yes
People in Hampshire live safe, healthy and independent lives:	yes
People in Hampshire enjoy a rich and diverse environment:	yes
People in Hampshire enjoy being part of strong, inclusive communities:	yes

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Due regard in this context involves having due regard in particular to:

a) The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;

b) Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;

c) Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionally low.

1.2. **Equalities Impact Assessment:**

A high level Equalities Impact Assessment has been undertaken. The grants are intended to have a positive impact and advance equality.

2. Impact on Crime and Disorder:

2.1 Not applicable.

3. Climate Change:

a) How does what is being proposed impact on our carbon footprint / energy consumption?

Not applicable.

b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

Not applicable.

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Quarterly Reporting of Surveillance

Number of Authorisations by Quarter (1 April 2018 – 31 March 2019)

Direct Surveillance			
	Purpose of Surveillance		
2018-19 Quarter	C'feit Goods	Under Age Sales	Other
1	0	0	0
2	0	0	0
3	0	0	0
4			
Total -	**0**	**0**	**0**
Covert Human Intelligence Source (CHIS)			
	Purpose of Surveillance		
Quarter	C'feit Goods	Under Age Sales	Other
1	0	0	0
2	1	0	0
3	1	0	0
4			
Total -	**2**	**0**	**0**

Communications Data			
Quarter	Number of Applications	Number of Specific Notices	Offences related to:
1	0	0	N/A
2	0	0	N/A
3	0	0	N/A
4			
Total -	**0**	**0**	**0**

The decision to deploy any of the surveillance techniques defined within RIPA is dependent upon many considerations. Where there are other investigative tools available, which are both overt in nature and more appropriate to be used, they will be deployed instead of reverting to any of the surveillance techniques referenced within RIPA.

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HAMPSHIRE COUNTY COUNCIL

Decision Report

Committee/Panel:	Audit Committee
Date:	21 February 2019
Title:	Treasury Management Strategy Statement 2019/20 to 2021/22
Report From:	Director of Corporate Resources – Corporate Services

Contact name: Andrew Boutflower

Tel: 01962 847407 **Email:** andrew.boutflower@hants.gov.uk

1. Recommendation

That the Audit Committee notes the following recommendations that have been made to Cabinet:

1.1. That the Treasury Management Strategy, including the Annual Investment Strategy for 2019/20 (and the remainder of 2018/19) is approved.

1.2. That authority is delegated to the Deputy Chief Executive and Director of Corporate Resources to manage the County Council's investments and borrowing according to the Treasury Management Strategy Statement as appropriate.

1.3. That a further £1m is added to the Investment Risk Reserve as protection against the irrecoverable fall in value of any investments.

2. Summary

2.1. The Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 (the CIPFA Code) requires authorities to determine the Treasury Management Strategy Statement (TMSS) before the start of each financial year. This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

3. Introduction

3.1. In 2018 the Ministry of Housing, Communities and Local Government produced new investment guidance for local authorities, including the requirement to produce an Investment Strategy. The Capital and Investment Strategy sets out the Council's broad approach to investment, including its capital programme, how this is funded, and investments held for service purposes or for commercial profit.

3.2. This treasury management strategy supports the Capital and Investment Strategy in setting out the arrangements for the management of the County Council's cash flows, borrowing and investments, and the associated risks. The County Council has borrowed and invested 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 financial risk are therefore central to the County Council's prudent financial management.

3.3. Treasury risk management at the County Council is conducted within the framework of the CIPFA Code which requires the County Council to approve a TMSS before the start of each financial year. This report fulfils the County Council's legal obligation under the Local Government Act 2003 to have regard to the CIPFA Code.

4. External Context

4.1. The following paragraphs explain the economic and financial background against which the TMSS is being set.

Economic background

4.2. The UK's progress negotiating its exit from the European Union, together with its future trading arrangements, will continue to be a major influence on the County Council's TMSS for 2019/20.

4.3. UK Consumer Price Inflation for October was up 2.4% year-on-year, slightly below the consensus forecast and broadly in line with the Bank of England's (BoE) November Inflation Report. The most recent labour market data for October 2018 showed the unemployment rate edged up slightly to 4.1% while the employment rate of 75.7% was the joint highest on record. The 3-month average annual growth rate for pay excluding bonuses was 3.3% as wages continue to rise steadily and provide some pull on general inflation. Adjusted for inflation, this means real wages grew by 1.0%, a level still likely to have little effect on consumer spending.

4.4. The rise in quarterly GDP growth to 0.6% in Quarter 3 from 0.4% in the previous quarter was due to weather-related factors boosting overall household consumption and construction activity over the summer following the weather-related weakness in Quarter 1. At 1.5%, annual Gross Domestic Product growth continues to remain below trend. Looking ahead, the BoE, in its November Inflation Report, expects GDP growth to average around 1.75% over the forecast horizon, providing the UK's exit from the EU is relatively smooth.

4.5. Following the BoE's decision to increase Bank Rate to 0.75% in August 2018, no changes to monetary policy have been made since. However, the Bank expects that should the economy continue to evolve in line with its November forecast, further increases in the Bank Rate will be required to return inflation to the 2% target. The Monetary Policy Committee (MPC) continues to reiterate that any further increases will be at a gradual pace and limited in extent.

Credit outlook

4.6. The big four UK banking groups have now divided their retail and investment banking divisions into separate legal entities under ringfencing legislation. Bank of Scotland, Barclays Bank UK, HSBC UK Bank, Lloyds Bank, National Westminster Bank, Royal Bank of Scotland and Ulster Bank are the ringfenced banks that now only conduct lower risk retail banking activities. Barclays Bank, HSBC Bank, Lloyds Bank Corporate Markets and NatWest Markets are the investment banks. Credit rating agencies have adjusted the ratings of some of these banks with the ringfenced banks generally being better rated than their non-ringfenced counterparts.

4.7. European banks are considering their approach to Brexit, with some looking to create new UK subsidiaries to ensure they can continue trading here. The credit strength of these new banks remains unknown, although the chance of parental support is assumed to be very high if ever needed. The uncertainty caused by protracted negotiations between the UK and EU is weighing on the creditworthiness of both UK and European banks with substantial operations in both jurisdictions.

Interest rate forecast

4.8. Following the increase in Bank Rate to 0.75% in August 2018, the Council's treasury management adviser Arlingclose is forecasting two more 0.25% rises during 2019 to take official UK interest rates to 1.25%. The BoE's MPC has maintained expectations for slow and steady rate rises over the forecast horizon. The MPC continues to have a bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. Arlingclose believes that MPC members consider both that ultra-low interest rates result in other economic problems, and that a higher Bank Rate will be a more effective policy weapon should downside Brexit risks crystallise when rate cuts will be required.

4.9. The UK economic environment remains relatively soft, despite seemingly strong labour market data. Arlingclose's view is that the economy still faces a challenging outlook as it exits the European Union and Eurozone growth softens. While assumptions are that a Brexit deal is struck and some agreement reached on transition and future trading arrangements before the UK leaves the EU, the possibility of a "no deal" Brexit still hangs over economic activity (at the time of writing this commentary in mid-December). As such, the risks to the interest rate forecast are considered firmly to the downside.

4.10. A more detailed economic and interest rate forecast provided by Arlingclose is attached at Appendix 1.

5. Balance Sheet Summary and Forecast

5.1. On 30 November 2018, the County Council held £278m of borrowing and £598m of investments. This is set out in further detail at Appendix B. Forecast changes in these sums are shown in the balance sheet analysis in Table 1 below.

Table 1: Balance sheet summary and forecast

	31/03/18 Actual £m	31/03/19 Estimate £m	31/03/20 Forecast £m	31/03/21 Forecast £m	31/03/22 Forecast £m
Capital Financing Requirement	764	794	813	816	796
Less: Other long-term liabilities					
- Street Lighting PFI	(56)	(53)	(50)	(46)	(42)
- Waste Management Contract	(108)	(104)	(100)	(96)	(91)
Borrowing CFR	600	637	663	674	663
Less: External borrowing					
- Public Works Loan Board	(243)	(236)	(227)	(217)	(208)
- Market Loans (incl. LOBOs)	(41)	(41)	(41)	(41)	(41)
Internal (over) borrowing	316	360	395	416	414
Less: Reserves and balances	(646)	(629)	(612)	(619)	(623)
Less: Allowance for working capital	(184)	(184)	(184)	(184)	(184)
Resources for investment	(830)	(813)	(796)	(803)	(807)
New Borrowing or (Investments)	(514)	(453)	(401)	(387)	(393)

5.2. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR), while usable reserves and working capital are the underlying resources available for investment. The County Council's current strategy is to maintain borrowing and investments below their underlying levels, sometimes known as internal borrowing.

5.3. It is forecast that the County Council will continue to take advantage of internal borrowing, which will increase, over the period forecast in Table 1, whilst paying off PWLB debt as maturities arise. Reserves and balances are due to reduce over the forecast period due to the anticipated funding of the capital programme, repayment of external debt, and use of the Grant Equalisation Reserve as part of the County Council's financial strategy. These factors result in a reducing investment balance year on year over the forecast period, as shown in Table 1.

5.4. CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the County Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the County Council expects to comply with this recommendation during 2019/20.

6. Borrowing Strategy

6.1. The County Council currently holds £278m of loans, a decrease of £16m on the previous year, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in Table 1 shows that the County Council does not expect to need to borrow in 2019/20. The County Council may however borrow to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £930m.

Objectives

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

Strategy

6.3. Given the significant cuts to public expenditure and in particular to local government funding, the County Council's borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio. With short-term interest rates currently much lower than long-term rates, if the County Council does need to borrow, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

6.4. By internally borrowing, the County Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. If borrowing is required, the benefits of internal and short-term borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise modestly. Arlingclose will assist the County Council with this 'cost of carry' and breakeven analysis.

6.5. Alternatively, the County Council may arrange forward starting loans during 2019/20, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.

6.6. In addition, the County Council may borrow short-term loans (normally for up to one month) to cover unplanned cash flow shortages.

Sources

6.7. The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and any successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- any other UK public sector body
- UK public and private sector pension funds (except Hampshire Pension Fund)

- capital market bond investors
- UK Municipal Bonds Agency plc and other special purpose companies created to enable local authority bond issues

Other sources of debt finance

6.8. In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- leasing
- hire purchase
- Private Finance Initiative
- sale and leaseback

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

LOBOs

6.10. The County Council holds £20m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the County Council has the option to either accept the new rate or to repay the loan at no additional cost. All of these loans have options during 2019/20, and although the County Council understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The County Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so. Total borrowing via LOBO loans will be limited to the current level of £20m.

Short-term and variable rate loans

6.11. These loans leave the Council exposed to the risk of short-term interest rate rises, which is monitored through the indicator on interest rate exposure in the treasury management indicators in section 7.

Debt rescheduling

6.12. The PWLB allows authorities to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The County Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

7. Investment Strategy

7.1. The County Council holds invested funds representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the County Council's investment balance has ranged between

£550m and £665m, although lower levels are expected in the forthcoming year, as shown in Table 1.

Objectives

7.2. The CIPFA Code requires the County 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 County 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.

Negative interest rates

7.3. If the UK enters into a recession in 2019/20, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

Strategy

7.4. Given the increasing risk and very low returns from short-term unsecured bank investments, the County Council aims to continue to diversify into more secure and/or higher yielding asset classes during 2019/20. This is especially the case for the estimated £410m that is available for longer-term investment. Approximately 86% of the County Council's surplus cash is invested so that it is not subject to bail-in risk, as it is invested in local authorities, registered providers, pooled property, equity and multi-asset funds, and secured bank bonds.

7.5. Of the remaining cash subject to bail-in risk, 6% is held in short-term notice accounts which are maturing before the end of the financial year, 80% is held in overnight money market funds and cash plus funds which are subject to a reduced risk of bail-in, and 14% is held in certificates of deposit which can be sold on the secondary market. This diversification is a continuation of the strategy adopted in 2015/16. Further detail is provided at Appendix B.

Investments targeting higher returns

7.6. Given the stability of the County Council's cash balances there was the opportunity during 2016/17 to increase the allocation for investments targeting higher returns, which will allow further diversification and increase the overall rate of return and the income contribution to the revenue budget. It was approved that the allocation targeting higher yields increase to £200m from £105m.

7.7. By the end of 2018/19 the County Council will have fully allocated the £200m targeted for higher yielding investments. As cash balances continue to rise, it is proposed that for 2019/20 this limit is increased to £235m.

7.8. Higher yields can be accessed through long-term cash investments (although this is currently less the case as yields have declined) and investments in other assets than cash, such as pooled property, equities and bonds. Non-cash pooled investments must be viewed as long-term investments in order that monies are not withdrawn in the event of a fall in capital values to avoid crystallising a capital loss.

7.9. When the County Council began to specifically target higher returns from a proportion of its investments, it also established an Investment Risk Reserve in order to mitigate the risk of an irrecoverable fall in the value of these investments. Given that the Council is increasing its exposure, having now reached its target, it is recommended that a further £1m is added to this reserve, to bring the total to £3m.

7.10. As shown in Appendix 2 the County Council had invested £156.8m of the £200m allocation as at 30 November 2018. In addition, the County Council has committed a further £43.2m to investments in pooled funds, which once invested will complete the allocation targeting higher yields. Without this allocation the weighted average return of the Council's cash investments would have been 1.21%; the allocation to higher yielding investments has added 0.99% (£5.9m based on the cash balance at 30 November 2018) to the average interest rate earned by the remainder of the portfolio.

7.11. Although money can usually be redeemed from the pooled funds at short notice, the County Council's intention is to hold them for at least the medium-term. Their performance and suitability in meeting the County Council's investment objectives are monitored regularly and discussed with Arlingclose.

Table 2: Pooled fund investments capital value at 30 November 2018

Pooled fund investments	Principal invested £m	Market value 30/11/18 £m	Capital yield (per annum) %
Pooled property	58.4	60.4	2.29
Pooled equity	43.4	44.8	(0.86)
Pooled multi-asset	20.0	19.5	(2.58)
Total	**121.8**	**124.6**	**0.36**

Investment limits

7.12. The maximum that will be lent to any one organisation (other than the UK Government) will be £70m. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, and investments in pooled funds, as they would not count against a limit for any single foreign country, since the risk is diversified over many countries.

Table 3: Investment limits

	Cash limit
Any single organisation, except the UK Central Government	£70m each
UK Central Government	unlimited
Any group of organisations under the same ownership	£70m per group
Any group of pooled funds under the same management	£70m per manager
Registered providers and registered social landlords	£70m in total
Money market funds	50% in total
Real estate investment trusts	£70m in total

Approved counterparties

7.13. The County Council may invest its surplus funds with any of the counterparty types in Table 4 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 4: Approved investment counterparties and limits

Credit Rating	Banks		Government	Corporates	Registered Providers	
	Unsecured	Secured			Unsecured	Secured
UK Govt	n/a	n/a	£ Unlimited 30 years	n/a	n/a	n/a
AAA	£35m 5 years	£70m 20 years	£70m 30 years	£35m 20 years	£35m 20 years	£35m 20 years
AA+	£35m 5 years	£70m 10 years	£70m 25 years	£35m 10 years	£35m 10 years	£35m 10 years
AA	£35m 4 years	£70m 5 years	£70m 15 years	£35m 5 years	£35m 10 years	£35m 10 years
AA-	£35m 3 years	£70m 4 years	£70m 10 years	£35m 4 years	£35m 10 years	£35m 10 years
A+	£35m 2 years	£70m 3 years	£35m 5 years	£35m 3 years	£35m 5 years	£35m 5 years
A	£35m 13 months	£70m 2 years	£35m 5 years	£35m 2 years	£35m 5 years	£35m 5 years
A-	£35m 6 months	£70m 13 months	£35m 5 years	£35m 13 months	£35m 5 years	£35m 5 years
None	£35m 6 months	n/a	£70m 25 years	n/a*	£35m 5 years	£35m 25 years
Pooled funds and real estate investment trusts	£70m per fund					

*see paragraph 6.19

This table must be read in conjunction with the notes below

Credit Rating

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

Banks Unsecured

7.15. Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. See below for arrangements relating to operational bank accounts.

Banks Secured

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

Government

7.17. Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is generally a lower risk of insolvency, although they are not zero risk. Investments with the UK Central Government may be made in unlimited amounts for up to 30 years.

Corporates

7.18. Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in but are exposed to the risk of the company going insolvent.

7.19. The County Council will not invest in an un-rated corporation except where it owns a controlling interest in the corporation, in which case a limit of £35m will for an investment of up to 20 years will apply.

Registered Providers Secured and Unsecured

7.20. Loans and bonds issued by, guaranteed by or secured on the assets of registered providers of social housing and registered social landlords. These bodies are tightly regulated by the Regulator of Social Housing (in England), the Scottish Housing Regulator, the Welsh Government, and the Department for Communities (in Northern Ireland). As providers of public services, they retain the likelihood of receiving government support if needed.

Pooled Funds

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

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

Real estate investment trusts (REITs)

7.23. Shares in companies that invest mainly in real estate and pay the majority of their rental income to investors in a similar manner to pooled property funds. As with property funds, REITs offer enhanced returns over the longer term, but are more volatile especially as the share price reflects changing demand for the shares as well as changes in the value of the underlying properties.

Operational bank accounts

7.24. The County Council may incur operational exposures, for example through current accounts, to any UK bank with credit ratings no lower than BBB- and with assets greater than £25 billion. These are not classed as investments, but are still subject to the risk of a bank bail-in, and balances will therefore be kept low. The County Council's operational bank account is with National Westminster and aims to keep the overnight balances held in current accounts positive, and as close to £0 as possible. The Bank of England has stated that in the event of failure, banks with assets greater than £25 billion are more likely to be bailed-in than made insolvent, increasing the chance of the County Council maintaining operational continuity.

Risk assessment and credit ratings

7.25. Credit ratings are obtained and monitored by the County Council's treasury advisers, who will notify changes in ratings as they occur. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

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

7.26. Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn on the next working day will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Other Information on the security of investments

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

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

Liquidity management

7.29. The County Council has due regard for its future cash flows when determining the maximum period for which funds may prudently be committed. Historic cash flows are analysed in addition to significant future cash movements, such as payroll, grant income and council tax precept. Limits on long-term investments are set by reference to the County Council's medium term financial position (summarised in Table 1) and forecast short-term balances.

8. Treasury Management Indicators

8.1. The County Council measures and manages its exposures to treasury management risks using the following indicators.

Interest rate exposures

8.2. The following indicator shows the sensitivity of the County Council's current investments and borrowing to a change in interest rates.

Table 5: Interest rate risk indicator

	30 November 2018	Impact of +/-1% interest rate change
Sums subject to variable interest rates		
Investment	£373.1m	+/-£3.7m
Borrowing	(£20.0m)	+/-£0.2m

Maturity structure of borrowing

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

Table 6: Refinancing rate risk indicator

	Upper	Lower
Under 12 months	50%	0%
12 months and within 24 months	50%	0%
24 months and within 5 years	50%	0%
5 years and within 10 years	75%	0%
10 years and within 20 years	75%	0%
20 years and within 30 years	75%	0%
30 years and above	100%	0%

8.4. 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.

Principal sums invested for periods longer than a year

8.5. The purpose of this indicator is to control the County Council'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 will be:

Table 7: Price risk indicator

	2019/20	2020/21	2021/22
Limit on principal invested beyond a year	£410m	£350m	£350m

9. Related matters

9.1. The CIPFA Code requires the County Council to include the following in its TMSS.

Financial derivatives

9.2. Local authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk (e.g.

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

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

9.4. Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit. The use of financial derivatives is not planned as part of the implementation of the TMSS and any changes to this would be reported to members in the first instance.

Investment Training

9.5. The needs of the County Council's treasury management staff for training in investment management are assessed annually as part of the staff appraisal process, and additionally when the responsibilities of individual members of staff change.

9.6. Staff regularly attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, and other appropriate organisations.

9.7. CIPFA's Code of Practice requires that the County Council ensures that all members tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive appropriate training relevant to their needs and understand fully their roles and responsibilities. All members were invited to a workshop presented by Arlingclose on 27 November 2018, which gave an update of treasury matters. A further Arlingclose workshop has been planned for November 2019.

Investment Advisers

9.8. The County Council has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is controlled through quarterly review meetings with the Deputy Chief Executive and Director of Corporate Resources' staff and Arlingclose.

Markets in Financial Instruments Directive

9.9. The County Council has opted up to professional client status with its providers of financial services, including advisers, brokers, and fund managers, allowing it access to a greater range of services but without the greater regulatory protections afforded to individuals and small companies. Given the size and range of the County Council’s treasury management activities, the s151 officer believes this to be the most appropriate status.

CORPORATE OR LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	No
People in Hampshire live safe, healthy and independent lives:	No
People in Hampshire enjoy a rich and diverse environment:	No
People in Hampshire enjoy being part of strong, inclusive communities:	no
OR	
This proposal does not link to the Strategic Plan but, nevertheless, requires a decision because: For the ongoing management of the County Council's investments and borrowing	

Other Significant Links

Links to previous Member decisions:	
Title	Date

Direct links to specific legislation or Government Directives	
Title	Date

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;

Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

1.2. **Due regard in this context involves having due regard in particular to:**

The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;

Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;

Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionally low.

1.3. **Equalities Impact Assessment:**

1.4. Equality objectives are not considered to be adversely affected by the proposals in this report.

2. Impact on Crime and Disorder:

2.1. The proposals in this report are not considered to have any direct impact on the prevention of crime.

3. Climate Change:

How does what is being proposed impact on our carbon footprint / energy consumption*?*

No specific impact.

How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

No specific impact.

Arlingclose Economic & Interest Rate Forecast October 2018

Underlying assumptions:

- The MPC left Bank Rate unchanged at the September meeting, after voting unanimously to increase Bank Rate to 0.75% in August.
- Our projected outlook for the UK economy means we maintain the significant downside risks to our interest rate forecast. The UK economic environment is relatively soft, despite seemingly strong labour market data. GDP growth recovered somewhat in Q2 2018, but the annual growth rate of 1.2% remains well below the long term average. Our view is that the UK economy still faces a challenging outlook as the country exits the European Union and Eurozone economic growth softens.
- Cost pressures were projected to ease but have risen more recently and are forecast to remain above the Bank's 2% target through most of the forecast period. The rising price of oil and tight labour market means inflation may remain above target for longer than expected. This means that strong real income growth is unlikely in the near future.
- The MPC has a bias towards tighter monetary policy but is reluctant to push interest rate expectations too strongly. We believe that MPC members consider both that: 1) ultra-low interest rates result in other economic problems, and 2) higher Bank Rate will be a more effective policy weapon should downside Brexit risks crystallise and cuts are required.
- The global economy appears to be slowing, particularly the Eurozone and China, where the effects of the trade war has been keenly felt. Despite slower growth, the European Central Bank is adopting a more strident tone in conditioning markets for the end of QE, the timing of the first rate hike (2019) and their path thereafter. Meanwhile, European political issues, mostly lately with Italy, continue.
- The US economy is expanding more rapidly. The Federal Reserve has tightened monetary policy by raising interest rates to the current 2%-2.25% range; further rate hikes are likely, which will start to slow economic growth. Central bank actions and geopolitical risks have and will continue to produce significant volatility in financial markets, including bond markets.

Forecast:

- The MPC has maintained expectations of a slow rise in interest rates over the forecast horizon. Our central case is for Bank Rate is to rise twice in 2019. The risks are weighted to the downside.

- Gilt yields have remained at low levels. We expect some upward movement from current levels based on our interest rate projections, the strength of the US economy and the ECB's forward guidance on higher rates. However, volatility arising from both economic and political events will continue to offer borrowing opportunities.

	Dec-18	Mar-19	Jun-19	Sep-19	Dec-19	Mar-20	Jun-20	Sep-20	Dec-20	Mar-21	Jun-21	Sep-21	Dec-21	Average
Official Bank Rate														
Upside risk	0.00	0.00	0.00	0.00	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.25	0.17
Arlingclose Central Case	0.75	1.00	1.00	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.25	1.17
Downside risk	0.00	0.50	0.50	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.65
3-mth money market rate														
Upside risk	0.10	0.10	0.10	0.10	0.15	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.20	0.17
Arlingclose Central Case	0.80	1.00	1.10	1.20	1.30	1.30	1.25	1.20	1.20	1.20	1.20	1.20	1.20	1.17
Downside risk	0.20	0.50	0.60	0.70	0.80	0.80	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.68
1-yr money market rate														
Upside risk	0.20	0.30	0.30	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.33
Arlingclose Central Case	1.05	1.25	1.35	1.40	1.50	1.45	1.40	1.40	1.40	1.40	1.40	1.40	1.40	1.37
Downside risk	0.35	0.50	0.60	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.75	0.69
5-yr gilt yield														
Upside risk	0.15	0.20	0.25	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.32
Arlingclose Central Case	1.15	1.20	1.25	1.35	1.40	1.40	1.35	1.35	1.30	1.30	1.30	1.30	1.30	1.30
Downside risk	0.30	0.35	0.45	0.50	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.54
10-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.32
Arlingclose Central Case	1.60	1.65	1.65	1.70	1.75	1.75	1.75	1.70	1.70	1.70	1.70	1.70	1.70	1.70
Downside risk	0.30	0.45	0.50	0.55	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.60	0.55
20-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.32
Arlingclose Central Case	1.90	1.95	1.95	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	2.00	1.98
Downside risk	0.30	0.40	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.43
50-yr gilt yield														
Upside risk	0.20	0.25	0.25	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.35	0.32
Arlingclose Central Case	1.80	1.85	1.85	1.90	1.90	1.90	1.90	1.90	1.90	1.90	1.90	1.90	1.90	1.88
Downside risk	0.30	0.40	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.45	0.43

PWLB Certainty Rate (Maturity Loans) = Gilt yield + 0.80%
PWLB Local Infrastructure Rate (Maturity Loans) = Gilt yield + 0.60%

Existing Investment & Debt Portfolio Position at 30 November 2018

Investments	30/09/2018 Balance £m	Movement £m	30/11/2018 Balance £m	30/11/2018 Rate %	30/11/2018 WAM* Years
Short term Investments					
Banks and Building Societies:					
Unsecured	20.5	(3.6)	16.9	0.72	0.31
Secured	52.4	-	52.4	1.14	0.22
Money Market Funds	21.1	23.4	44.5	0.73	0.01
Cash Plus Funds	20.0	-	20.0	0.59	n/a
Local Authorities	122.0	16.5	138.5	1.34	0.47
Registered Provider	20.0	-	20.0	2.30	0.16
	256.0	36.3	292.3	1.22	0.32
Long term Investments					
Banks and Building Societies:					
Secured	78.3	-	78.3	1.06	2.40
Local Authorities	81.0	(10.0)	71.0	1.33	2.45
	159.3	(10.0)	149.3	1.20	2.42
Long term Investments – high yielding strategy					
Local Authorities					
Fixed deposits	20.0	-	20.0	3.96	15.30
Fixed bonds	10.0	-	10.0	3.78	15.11
Pooled Funds					
Pooled property**	55.0	3.4	58.4	4.19	n/a
Pooled equity**	40.0	3.4	43.4	5.80	n/a
Pooled multi-asset**	20.0	-	20.0	7.15	n/a
Registered Provider	5.0	-	5.0	3.40	0.41
	150.0	6.8	156.8	4.93	13.12
TOTAL INVESTMENTS	**565.3**	**33.1**	**598.4**	**2.20**	**1.99**

* Weighted average maturity

** The rates provided for pooled fund investments are reflective of the average of the most recent dividend return as at 30 November 2018.

	£m	%
External Borrowing		
PWLB Fixed Rate	(237.2)	(4.69)
LOBO Loans	(20.0)	(4.76)
Other Market Loans	(21.0)	(4.01)
Total External Borrowing	(278.2)	(4.64)
Other Long-Term Liabilities:		
Street Lighting PFI	(107.9)	
Waste Management Contract	(56.3)	
Total Other Long-Term Liabilities	(164.2)	
Total Gross External Debt	**(442.4)**	
Investments	**598.4**	**2.20**
Net (Debt) / Investments	**156.0**	

HAMPSHIRE COUNTY COUNCIL

Report

Committee/Panel:	Audit Committee
Date:	21 February 2019
Title:	Hampshire County Council Audit Planning Report – 2018/19
Report From:	External Auditors – Ernst and Young

Contact name: Martin Young

Tel: 02380 382220 **Email:** myoung1@uk.ey.com

1. Recommendation

1.1 That the Audit Committee receives and notes the Hampshire County Council Audit Planning Report for 2018/19 as attached at Appendix 1.

CORPORATE OR LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	yes
People in Hampshire live safe, healthy and independent lives:	yes
People in Hampshire enjoy a rich and diverse environment:	yes
People in Hampshire enjoy being part of strong, inclusive communities:	yes

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Due regard in this context involves having due regard in particular to:

a) The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;

b) Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;

c) Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionally low.

1.2. **Equalities Impact Assessment:**

A high level Equalities Impact Assessment has been undertaken. The grants are intended to have a positive impact and advance equality.

2. Impact on Crime and Disorder:

2.1 Not applicable.

3. Climate Change:

a) How does what is being proposed impact on our carbon footprint / energy consumption?

Not applicable.

b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

Not applicable.

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Hampshire County Council

Audit planning report

Year ended 31 March 2019

January 2019

Building a better working world

Private and Confidential

22nd January 2019

Audit Committee
Hampshire County Council
The Castle
Winchester
Hampshire
SO23 8UJ

Dear Members

Audit planning report

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as your auditor. Its purpose is to provide the Audit Committee with a basis to review our proposed audit approach and scope for the 2018/19 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This Plan summarises our initial assessment of the key risks driving the development of an effective audit for the Council, and outlines our planned audit strategy in response to those risks.

This report is intended solely for the information and use of the Audit Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss this report with you on 21st February 2019 as well as understand whether there are other matters which you consider may influence our audit.

Yours faithfully

Maria Grindley

Associate Partner

For and on behalf of Ernst & Young LLP

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Public Sector Audit Appointments Ltd (PSAA) issued the "Statement of responsibilities of auditors and audited bodies". It is available from the PSAA website (https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/).The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The "Terms of Appointment and further guidance (updated April 2018)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Audit Committee and management of Hampshire County Council in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, and management of Hampshire County Council those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee and management of Hampshire County Council for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.

01 Overview of our 2018/19 audit strategy

Overview of our 2018/19 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Audit risks and areas of focus			
Risk / area of focus	**Risk identified**	**Change from PY**	**Details**
Misstatements due to fraud or error	Fraud risk	No change in risk or focus	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively. In addition to our overall response, we consider where these risks may manifest themselves and identify separate fraud risks as necessary below. We concluded that only those procedures included under 'Inappropriate capitalisation of revenue expenditure' are required.
Inappropriate capitalisation of revenue expenditure	Fraud risk	No change in risk - separately identified in 2018/19	Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10 issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition. Our judgement is that this risk at this Council relates to the improper capitalisation of revenue expenditure.
Valuation of Land and Buildings and Investment Properties	Higher inherent risk	No change in risk or focus.	Property, Plant and Equipment Land and Buildings (L&B) and Investment Properties (IP) represent significant balances in the Council's accounts and are subject to valuation changes, impairment reviews and depreciation charges. Material judgemental inputs and estimation techniques are required to calculate the year-end L&B and IP balances held in the balance sheet. As the Council's asset base is significant, and the outputs from the valuer are subject to estimation, there is a higher inherent risk that L&B and IP may be under/overstated or the associated accounting entries incorrectly posted. We are required us to undertake procedures on the use of experts and assumptions underlying fair value estimates.

Overview of our 2018/19 audit strategy

Risk / area of focus	Risk identified	Change from PY	Details
Pension Accounting	Higher inherent Risk	No change in risk of focus	The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Hampshire County Council. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2018 this totalled £1,340 million. The information disclosed is based on the IAS 19 report issued by the actuary to the County Council. Accounting for these schemes involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. We are required to undertake procedures on the use of experts and the assumptions underlying fair value estimates.
New Accounting Standards	Inherent risk	New risk identified this year.	IFRS 9 (Financial Instruments) and IFRS 15 (Revenue from contracts) apply from 1 April 2018. We will review the Council's assessment of the impact of these new standards to determine whether they have been appropriately implemented.

Materiality

Planning materiality
£38.2m

Planning materiality has been set at £38,222,000 which represents 1.8% of 2017/18 gross expenditure

Performance materiality
£28.7m

Performance materiality has been set at £28,666,000 which represents 75% of Planning Materiality

Audit differences
£1.9m

We will report all uncorrected misstatements relating to the income statement and balance sheet that have an effect on income and misstatements in the OCI over £1,911,000. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2018/19 audit strategy

Audit scope

This Audit Plan covers the work that we plan to perform to provide you with:

- our audit opinion on whether the financial statements of Hampshire County Council give a true and fair view of the financial position as at 31 March 2019 and of the income and expenditure for the year then ended; and
- our conclusion on the Council's arrangements to secure economy, efficiency and effectiveness;

We will also review and report to the National Audit Office (NAO), to the extent and in the form required by them, on the Council's Whole of Government Accounts return.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- strategic, operational and financial risks relevant to the financial statements;
- developments in financial reporting and auditing standards;
- the quality of systems and processes;
- changes in the business and regulatory environment; and
- management's views on all of the above.

By considering these inputs, our audit focuses on the areas that matter and our feedback is more likely to be relevant to the Council.

We will provide an update to the Audit Committee on the results of our work in these areas in our report to those charged with governance scheduled for delivery in July 2019.

02 Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Misstatements due to fraud or error

Financial statement impact

Misstatements that occur in relation to the risk of fraud due to management override could affect a number of areas of the financial statements.

What is the risk?

As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively.

We identify and respond to this risk on every audit engagement.

What will we do?

- Inquire of management about risks of fraud and the controls put in place to address those risks.
- Understand the oversight given by those charged with governance of management's processes over fraud.
- Consider of the effectiveness of management's controls designed to address the risk of fraud.

Perform mandatory procedures regardless of specifically identified fraud risks, including:

- Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements
- Assessing accounting estimates for evidence of management bias, and
- Evaluating the business rationale for significant unusual transactions.

We will utilise our data analytics capabilities to assist with our work.

Having evaluated this risk we have considered whether we need to perform other audit procedures not referred to above. We concluded that only those procedures included under 'Inappropriate capitalisation of revenue expenditure' are required.

Our response to significant risks

We have set out the significant risks identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Inappropriate capitalisation of revenue expenditure

Financial statement impact

Misstatements that occur in relation to the risk of fraud in revenue and expenditure recognition could affect the income accounts. The relevant accounts we associate the revenue and expenditure recognition risk to had the following balances in the 2017-18 financial statements:

Cost of services expenditure: £2,028 million

PPE additions: £167.7million

What is the risk?

Under ISA 240 there is a presumed risk that revenue may be misstated due to improper revenue recognition. In the public sector, this requirement is modified by Practice Note 10, issued by the Financial Reporting Council, which states that auditors should also consider the risk that material misstatements may occur by the manipulation of expenditure recognition.

The risk in local government is in areas where management make judgements that impact whether material items of expenditure are financed from capital or revenue resources. This would be effected by management override of journal controls.

As such we associate this risk with capital additions.

What will we do?

For a sample of recorded capital additions we will examine invoices, capital expenditure authorisations and other data that support the appropriateness of these additions.

We will ensure that the items are capital in nature, and do not include revenue items.

We will utilise our data analytics capabilities to assist with our work through identifying high risk transactions, such as items originally recorded as revenue expenditure and subsequently capitalised.

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

What is the risk/area of focus?	What will we do?
Valuation of Land & Buildings and Investment Property Land and Buildings is the most significant balance in the Council's Balance Sheet. The valuation of Land and Buildings (L&B) and Investment Property (IP) is complex and subject to a number of assumptions and judgements. A small movement in these assumptions can have a material impact on the financial statements.	We will: • Consider the competence, capability and objectivity of the Council's valuer; • Consider the scope of the valuer's work; • Ensure L&B assets have been revalued within a 5 year rolling programme as required by the Code; • Ensure IP has been annually revalued as required by the Code; • Consider if there are any specific changes to assets that should have been communicated to the valuer; • Sample test key inputs used by the valuer when producing valuations; • Consider the results of the valuer's work; • Challenge the assumptions used by the Council's valuer by reference to external evidence and our EY valuation specialists (where necessary); • Test journals for the valuation adjustments to confirm that they have been accurately processed in the financial statements; • Test a sample of assets revalued in year to confirm that the valuation basis is appropriate and the accounting entries are correct; and • Review assets that are not subject to valuation in 2018/19 to confirm the remaining asset base is not materially misstated.

Audit risks

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

What is the risk/area of focus?	What will we do?
<u>Pension Liability Valuation</u> The Local Authority Accounting Code of Practice and IAS19 require the Council to make extensive disclosures within its financial statements regarding its membership of the Local Government Pension Scheme administered by Hampshire County Council. The Council's pension fund deficit is a material estimated balance and the Code requires that this liability be disclosed on the Council's balance sheet. At 31 March 2018 this totalled £1,340 million. The information disclosed is based on the IAS 19 report issued by the actuary to the County Council. Accounting for these schemes involves significant estimation and judgement and therefore management engages an actuary to undertake the calculations on their behalf. ISAs (UK) 500 and 540 require us to undertake procedures on the use of management experts and the assumptions underlying fair value estimates.	We will: • Liaise with the auditors of Hampshire Pension Fund, to obtain assurances over the information supplied to the actuary in relation to the Council's scheme members; • Assess the work of the LGPS Pension Fund actuary (Aon Hewitt) including the assumptions they have used by relying on the work of PWC - Consulting Actuaries commissioned by the National Audit Office for all Local Government sector auditors, and considering any relevant reviews by the EY actuarial team; • Review Hampshire Pension Fund's financial statements and compare the year end asset value with the estimate used by the actuary when producing the Council's IAS 19 report; and • Review and test the accounting entries and disclosures made within the Council's financial statements in relation to IAS19.

Audit risks

Other areas of audit focus (continued)

What is the risk/area of focus?	What will we do?
New Accounting standards	
IFRS 9 financial instruments This new accounting standard is applicable from the 2018/19 financial year and will change: • How financial assets are classified and measured; • How the impairment of financial assets are calculated; and • The disclosure requirements for financial assets. There are transitional arrangements within the standard; and the 2018/19 CIPFA Code of Practice on Local Authority accounting provides guidance on the application of IFRS 9.	We will: • Review implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19; • Consider whether relevant assets have been appropriately classified and valued; • Review new expected credit loss model impairment calculations for assets; and • Ensure that, subject to materiality, additional disclosure requirements have been met.
IFRS 15 Revenue from contracts with customers This new accounting standard is applicable from the 2018/19 financial year. The key requirements of the standard cover the identification of performance obligations under customer contracts and the linking of income to the meeting of those performance obligations. The 2018/19 CIPFA Code of Practice on Local Authority accounting provides guidance on the application of IFRS 15 and includes a useful flow diagram and commentary on the main sources of local government revenue and how they should be recognised. The impact on the County Council's accounting is likely to be limited as large revenue streams like council tax and government grants will be outside the scope of IFRS 15. However where that standard is relevant, the recognition of revenue will change and new disclosure requirements introduced.	We will: • Review implementation arrangements that should include an impact assessment paper setting out the application of the new standard, transitional adjustments and planned accounting for 2018/19; • Consider application to revenue streams, and where the standard is relevant test to ensure revenue is recognised when (or as) it satisfies a performance obligation; and • Ensure that, subject to materiality, additional disclosure requirements have been met.

03 Value for Money Risks

Value for Money

Background

We are required to consider whether the Council has put in place ‘proper arrangements’ to secure economy, efficiency and effectiveness on its use of resources. This is known as our value for money conclusion.

For 2018-19 this is based on the overall evaluation criterion:

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

Proper arrangements are defined by statutory guidance issued by the National Audit Office. They comprise your arrangements to:

- Take informed decisions;
- Deploy resources in a sustainable manner; and
- Work with partners and other third parties.

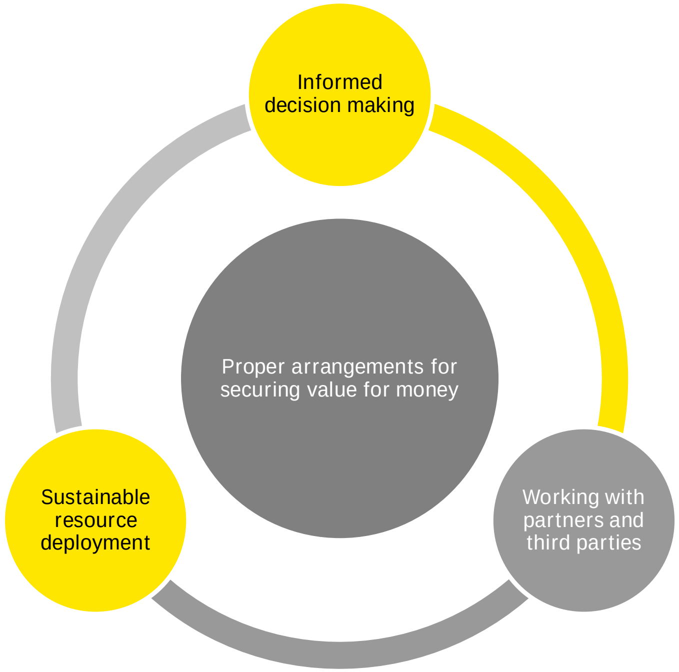
In considering your proper arrangements, we will draw on the requirements of the CIPFA/SOLACE framework for local government to ensure that our assessment is made against a framework that you are already required to have in place and to report on through documents such as your annual governance statement.

We are only required to determine whether there are any risks that we consider significant, which the Code of Audit Practice defines as:

“A matter is significant if, in the auditor’s professional view, it is reasonable to conclude that the matter would be of interest to the audited body or the wider public”

Our risk assessment supports the planning of sufficient work to enable us to deliver a safe conclusion on arrangements to secure value for money and enables us to determine the nature and extent of further work that may be required. If we do not identify any significant risks there is no requirement to carry out further work. We consider business and operational risks insofar as they relate to proper arrangements at both sector and organisation-specific level. In 2018/19 this has included consideration of the steps taken by the Council to consider the impact of Brexit on its future service provision, medium-term financing and investment values. Although the precise impact cannot yet be modelled, we anticipate that Authorities will be carrying out scenario planning and that Brexit and its impact will feature on operational risk registers.

Our risk assessment has therefore considered both the potential financial impact of the issues we have identified, and also the likelihood that the issue will be of interest to local taxpayers, the Government and other stakeholders. This has resulted in the identification of no significant risks which we view as relevant to our value for money conclusion. We will continue to update our risk assessment throughout the course of our audit.



04 Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2018/19 has been set at £38,222,000. This represents 1.8% of the Council's prior year gross expenditure. It will be reassessed throughout the audit process and once the draft 2018/19 statements have been prepared. This is based on the rationale that's public sector organisation do not have a focus on earnings profits. We consider industry factors, and using gross revenue expenditure is the industry norm.

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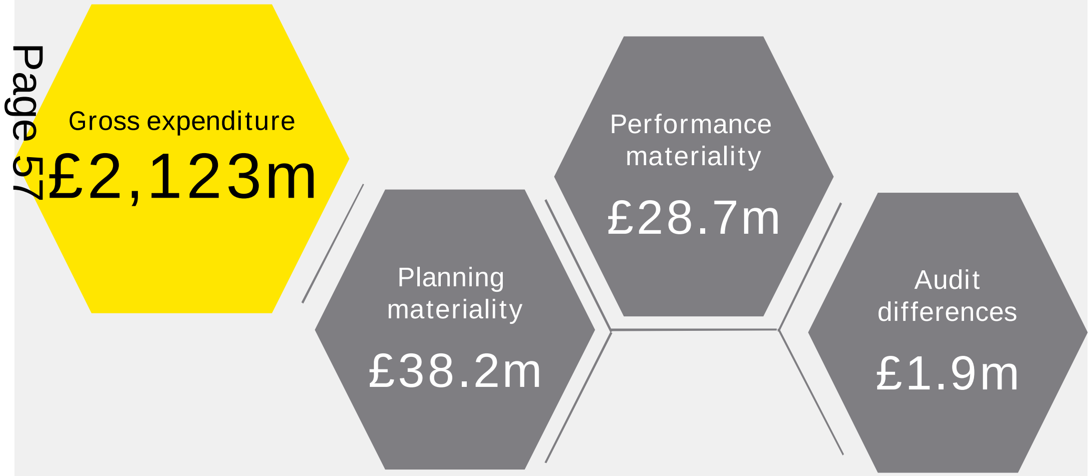

We request that the Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

Key definitions

Planning materiality – the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Performance materiality – the amount we use to determine the extent of our audit procedures. We have set performance materiality at £28,666,000 which represents 75% of planning materiality. We apply 75% when it is not an initial audit and we have a sound understanding of the entity and past experience with the engagement indicates that a higher risk of misstatement is unlikely.

Audit difference threshold – we propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the income statement and balance sheet that have an effect on income or that relate to other comprehensive income.

Other uncorrected misstatements, such as reclassifications and misstatements in the cashflow statement or disclosures and corrected misstatements will be communicated to the extent that they merit the attention of the Audit Committee, or are important from a qualitative perspective.

Specific materiality – We have set a materiality of £1k for officers and senior employees' remuneration and audit fees disclosures. This reflects our understanding that an amount less than our materiality would influence the economic decisions of users of the financial statements in relation to these.

05 Scope of our audit

Our Audit Process and Strategy

Objective and Scope of our Audit scoping

Under the Code of Audit Practice our principal objectives are to review and report on the Council's financial statements and arrangements for securing economy, efficiency and effectiveness in its use of resources to the extent required by the relevant legislation and the requirements of the Code.

We issue an audit report that covers:

1. Financial statement audit

Our objective is to form an opinion on the financial statements under International Standards on Auditing (UK).

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

- Addressing the risk of fraud and error;
- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

Procedures required by the Code

- Reviewing, and reporting on as appropriate, other information published with the financial statements, including the Annual Governance Statement; and
- Reviewing and reporting on the Whole of Government Accounts return, in line with the instructions issued by the NAO.

2. Arrangements for securing economy, efficiency and effectiveness (value for money)

We are required to consider whether the Council has put in place 'proper arrangements' to secure economy, efficiency and effectiveness on its use of resources.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls; and
- Substantive tests of detail of transactions and amounts.

Our initial assessment of the key processes across the Council has identified the following key processes where we will seek to rely on controls, both manual and IT:

- Accounts receivable;
- Accounts payable;
- Payroll;
- Cash and Bank;
- SWIFT social care; and
- CONFIRM highway maintenance.

We will use staff with specialised knowledge from EY's Financial Audit IT (FAIT) team to assist with our work on IT processes and controls.

Analytics:

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Audit Committee.

Internal audit:

We will regularly meet with the Head of Internal Audit, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan where they raise issues that could have an impact on the financial statements.

06 Audit team

Audit team

Audit team structure:

- Maria Grindley* Associate Partner
- Martin Young Manager
- Jack Dunkley Assistant Manager
- Maria Davison Senior

EY Properties (as applicable) | EY Actuaries | EY Financial Audit IT (FAIT)

Working together with the Council

We are working together with officers to identify continuing improvements in communication and processes for the 2018/19 audit.

We will continue to keep our audit approach under review to streamline it where possible.

* Key Audit Partner

Audit team

Use of specialists

When auditing key judgements, we are often required to use the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where EY specialists are expected to provide input for the current year audit are:

Area	Specialists
Pension valuation	Management Specialist – AoN Hewitt PwC (Consulting Actuary to the NAO) EY Specialist - EY actuaries
PFI valuation	Management Specialist - Capita
PPE valuation	Management Specialist - Management's in-house valuation experts EY Specialist - EY real estates (if necessary)

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Council's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

07 Audit timeline

Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2018/19.

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

Audit phase	Timetable	Audit committee timetable	Deliverables
Planning: Risk assessment and setting of scopes.	November		
Walkthrough of key systems and processes	November - December		
Testing of routine processes and controls	February	Audit Committee	Audit Planning Report
FAIT IT Systems Testing visit 1	February		
Interim audit testing	February - March		
FAIT IT Systems Testing visit 2	April		
Year end audit Audit Completion procedures	June/July	Audit Committee	Audit Results Report Audit opinions and completion certificates
Year end audit Audit Completion procedures	July / August	Audit Committee	Annual Audit Letter

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08 Independence

Introduction

The FRC Ethical Standard and ISA (UK) 260 “Communication of audit matters with those charged with governance”, requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in June 2016, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	**Final stage**
► The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between the you, your affiliates and directors and us; ► The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ► The overall assessment of threats and safeguards; ► Information about the general policies and process within EY to maintain objectivity and independence. ► Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard	► In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ► Details of non-audit services provided and the fees charged in relation thereto; ► Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ► Written confirmation that all covered persons are independent; ► Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy; ► Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and ► An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements, the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.

Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non –audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Maria Grindley, your audit engagement partner and the audit engagement team have not been compromised.

Self interest threats

A self interest threat arises when EY has financial or other interests in the Council. Examples include where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees. [

We believe that it is appropriate for us to undertake permissible non-audit services and we will comply with the policies that you have approved.

None of the services are prohibited under the Financial Reporting Council's Ethical Standard or the National Audit Office's Auditor Guidance Note 01 and you have no policy on pre-approval. The ratio of non audit fees to audits fees is not permitted to exceed 70%.

At the time of writing, the current ratio of non-audit fees to audit fees is approximately 48%. All fees are set out in Appendix A.

The only non-audit fees relate to a Readiness Assessment and independent Service Organisation Controls Type 1 Assurance Report for the Hampshire Integrated Business Centre (IBC).

From 2019/20 (and future years), the Council would like to obtain independent third party assurances over the financial reporting controls in place at the IBC. This is in respect of services provided to the IBC's clients. Preparation in 2018/19 is in the following phases:

- the Council has asked us to perform a 'Readiness Assessment' at the IBC (also known as a 'Gap Assessment'). We will identify key risks, associated controls and identify any gaps in existing controls;
- on completion of the Readiness Assessment (and any necessary remediation by the IBC) we have been asked to perform an independent Service Organisation Controls (SOC) 1 Type 1 assurance engagement as at 31st March 2019. This will be performed under the International Standard for Assurance Engagements (ISAE) No. 3402 issued by the International Auditing and Assurance Standards Board (IAASB). As this will be a Type 1 engagement, our review will focus on the design of controls only as at 31st March 2019. We expect to issue our ISAE 3402 Type 1 report in April 2019.

To ensure our independence as external auditor to Hampshire County Council is not impaired we are required to seek approval from PSAA (Public Sector Audit Appointments Ltd) to provide these non-audit services. This approval has been received.

In subsequent years (i.e. 2019/20 and future years), Council would like to obtain an independent Service Organisation Controls (SOC) 1 Type 2 assurance report covering the relevant financial year. This will need to be performed under the International Standard for Assurance Engagements (ISAE) No. 3402 issued by the International Auditing and Assurance Standards Board (IAASB). As this will be a Type 2 engagement, the review will focus on the design and operating effectiveness of controls for the relevant financial year.

We have adopted the following safeguards as a result. The work will be led and delivered by a separate Service Organisation Controls (SOC) reporting team. Members of the existing audit team at Hampshire County Council will not work on this project.

Relationships, services and related threats and safeguards

Self interest threats (continued)

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4. There are no other self interest threats at the date of this report.

Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no self review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of the Council. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

There are no management threats at the date of this report.

Other threats

Other threats, such as advocacy, familiarity or intimidation, may arise.

There are no other threats at the date of this report.

Other communications

EY Transparency Report 2018

Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained.

Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the year ended 1 July 2018 and can be found here:

http://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018

09 Appendices

Appendix A

Fees

The duty to prescribe fees is a statutory function delegated to Public Sector Audit Appointments Ltd (PSAA) by the Secretary of State for Communities and Local Government.

PSAA has published a scale fee for all relevant bodies. This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the NAO Code.

	Planned fee 2018/19	Scale fee 2018/19	Final Fee 2017/18
		£	£
Total Fee	89,720*	89,720*	116,519
Total audit	89,720*	89,720*	116,519
Other non-audit services**	43,000	N/A	N/A
Total other non-audit services	43,000	N/A	N/A
Total fees	132,720		116,519

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All fees exclude VAT

*PSAA has set the 2018/19 fee scale on the basis that individual scale audit fees for all opted-in bodies have been reduced by 23 per cent from the fees applicable for 2017/18. This gives opted-in bodies the benefit of the cost savings achieved in the recent audit procurement.

**Non audit services relate the Readiness Assessment and independent Service Organisation Controls Type 1 Assurance Report for the Hampshire Integrated Business Centre (IBC) only. For further details, see Section 8 (page 28). The fee is being funded by the Shared Services Partnership not directly by Hampshire County Council

The agreed fee presented is based on the following assumptions:

► Officers meeting the agreed timetable of deliverables;

► Our accounts opinion and value for money conclusion being unqualified;

► Appropriate quality of documentation is provided by the Council; and

► The Council has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Council in advance.

Fees for the auditor's consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Appendix B

Required communications with the Audit Committee

We have detailed the communications that we must provide to the Audit Committee .

		Our Reporting to you
Required communications	What is reported?	When and where
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit planning report
Significant findings from the audit	• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures • Significant difficulties, if any, encountered during the audit • Significant matters, if any, arising from the audit that were discussed with management • Written representations that we are seeking • Expected modifications to the audit report • Other matters if any, significant to the oversight of the financial reporting process	Audit results report
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: • Whether the events or conditions constitute a material uncertainty • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements • The adequacy of related disclosures in the financial statements	Audit results report
Misstatements	• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation • The effect of uncorrected misstatements related to prior periods • A request that any uncorrected misstatement be corrected • Corrected misstatements that are significant • Material misstatements corrected by management	Audit results report

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	What is reported?	When and where
Fraud	• Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity • Any fraud that we have identified or information we have obtained that indicates that a fraud may exist • A discussion of any other matters related to fraud	Audit results report
Related parties	• Significant matters arising during the audit in connection with the entity's related parties including, when applicable: • Non-disclosure by management • Inappropriate authorisation and approval of transactions • Disagreement over disclosures • Non-compliance with laws and regulations • Difficulty in identifying the party that ultimately controls the entity	Audit results report
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: • The principal threats • Safeguards adopted and their effectiveness • An overall assessment of threats and safeguards • Information about the general policies and process within the firm to maintain objectivity and independence	Audit Planning Report Audit Results Report
External confirmations	• Management's refusal for us to request confirmations • Inability to obtain relevant and reliable audit evidence from other procedures	Audit results report

Appendix B

Required communications with the Audit Committee (continued)

Required communications	What is reported?	Our Reporting to you — When and where
Consideration of laws and regulations	• Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off • Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	Audit results report
Internal controls	• Significant deficiencies in internal controls identified during the audit	Audit results report
Representations	Written representations we are requesting from management and/or those charged with governance	Audit results report
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report
Auditors report	• Any circumstances identified that affect the form and content of our auditor's report	Audit results report
Fee Reporting	• Breakdown of fee information when the audit plan is agreed • Breakdown of fee information at the completion of the audit • Any non-audit work	Audit planning report Audit results report
Certification work	Summary of certification work undertaken	Certification report

Appendix C

Additional audit information

Other required procedures during the course of the audit

In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.

Our responsibilities required by auditing standards	• Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. • Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Council's internal control. • Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management. • Concluding on the appropriateness of management's use of the going concern basis of accounting. • Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation. • Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Council to express an opinion on the financial statements. Reading other information contained in the financial statements, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and • Maintaining auditor independence.

Additional audit information (continued)

Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines:

- The locations at which we conduct audit procedures to support the opinion given on the financial statements; and
- The level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

HAMPSHIRE COUNTY COUNCIL

Report

Committee/Panel:	Audit Committee
Date:	21 February 2019
Title:	Hampshire Pension Fund Audit Planning Report – 2018/19
Report From:	External Auditors – Ernst and Young

Contact name: Martin Young

Tel: 02380 382220 **Email:** myoung1@uk.ey.com

1. Recommendation

1.1 That the Audit Committee receives and notes the Hampshire Pension Fund Audit Planning Report for 2018/19 as attached at Appendix 1.

CORPORATE OR LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	yes
People in Hampshire live safe, healthy and independent lives:	yes
People in Hampshire enjoy a rich and diverse environment:	yes
People in Hampshire enjoy being part of strong, inclusive communities:	yes

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Due regard in this context involves having due regard in particular to:

a) The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;

b) Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;

c) Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionally low.

1.2. **Equalities Impact Assessment:**

A high level Equalities Impact Assessment has been undertaken. The grants are intended to have a positive impact and advance equality.

2. Impact on Crime and Disorder:

2.1 Not applicable.

3. Climate Change:

a) How does what is being proposed impact on our carbon footprint / energy consumption?

Not applicable.

b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

Not applicable.

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Hampshire Pension Fund

Audit planning report

Year ended 31 March 2019

January 2019

Building a better working world

22nd January 2019

Audit Committee
Hampshire Pension Fund
The Castle
Winchester
Hampshire
SO23 8UJ

Dear Committee Members

Audit planning report

We are pleased to attach our Audit Plan which sets out how we intend to carry out our responsibilities as your auditor. Its purpose is to provide the Audit Committee with a basis to review our proposed audit approach and scope for the 2018/19 audit in accordance with the requirements of the Local Audit and Accountability Act 2014, the National Audit Office's 2015 Code of Audit Practice, the Statement of Responsibilities issued by Public Sector Audit Appointments (PSAA) Ltd, auditing standards and other professional requirements. It is also to ensure that our audit is aligned with the Committee's service expectations.

This plan summarises our initial assessment of the key risks driving the development of an effective audit for Hampshire Pension Fund, and outlines our planned audit strategy in response to those risks.

This report is intended solely for the information and use of the Audit Committee and management, and is not intended to be and should not be used by anyone other than these specified parties.

We welcome the opportunity to discuss this report with you on 21st February 2019 as well as understand whether there are other matters which you consider may influence our audit.

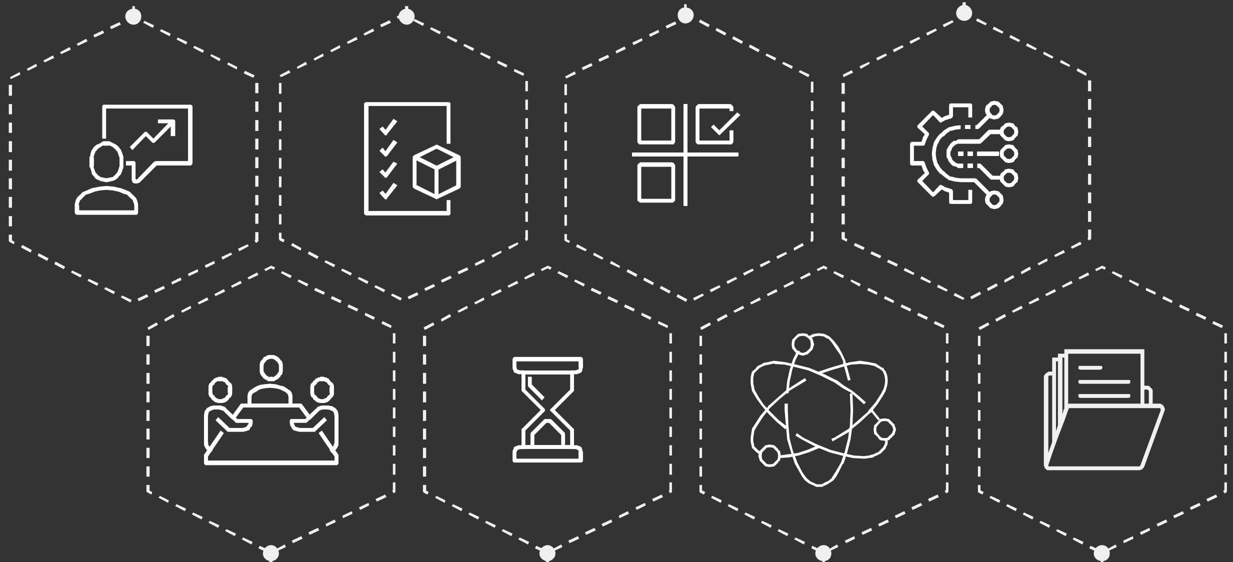
Yours faithfully

Maria Grindley

Associate Partner

For and on behalf of Ernst & Young LLP

Contents



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Public Sector Audit Appointments Ltd (PSAA) issued the "Statement of responsibilities of auditors and audited bodies". It is available from the PSAA website (https://www.psaa.co.uk/audit-quality/statement-of-responsibilities/).The Statement of responsibilities serves as the formal terms of engagement between appointed auditors and audited bodies. It summarises where the different responsibilities of auditors and audited bodies begin and end, and what is to be expected of the audited body in certain areas.

The "Terms of Appointment and further guidance (updated April 2018)" issued by the PSAA sets out additional requirements that auditors must comply with, over and above those set out in the National Audit Office Code of Audit Practice (the Code) and in legislation, and covers matters of practice and procedure which are of a recurring nature.

This report is made solely to the Audit Committee and management of Hampshire Pension Fund in accordance with the statement of responsibilities. Our work has been undertaken so that we might state to the Audit Committee, and management of Hampshire Pension Fund those matters we are required to state to them in this report and for no other purpose. To the fullest extent permitted by law we do not accept or assume responsibility to anyone other than the Audit Committee and management of Hampshire Pension Fund for this report or for the opinions we have formed. It should not be provided to any third-party without our prior written consent.

01 Overview of our 2018/19 audit strategy

Overview of our 2018/19 audit strategy

The following 'dashboard' summarises the significant accounting and auditing matters outlined in this report. It seeks to provide the Audit Committee with an overview of our initial risk identification for the upcoming audit and any changes in risks identified in the current year.

Audit risks and areas of focus

Risk / area of focus	Risk identified	Change from PY	Details
Misstatements due to fraud or error	Fraud risk	No change in risk of focus	As identified in ISA 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that would otherwise appear to be operating effectively
Risk of manipulation of investment valuation	Fraud risk	No change in risk – risk separately identified this year	As noted above, under ISA 240, management is in a unique position to perpetrate fraud through the override of controls. We have considered the main areas where management may have the incentive and opportunity to do this. At a Pension Fund, we have assessed that the risk of misstatement of investment valuation through management override of controls as the most likely areas of manipulation, and that this would occur specifically through journal postings.
Valuation of complex Investments (Level 3 Fair Value hierarchy)	Significant risk	New risk	Investments at Level 3 are those where at least one input that could have a significant effect on the asset's valuation is not based on observable market data. Significant judgements are made by the Investment Managers or administrators to value these investments whose prices are not publically available. The material nature of Investments means that any error in judgement could result in a material valuation error. Market volatility means such judgments can quickly become outdated, especially when there is a significant time period between the latest available audited information and the fund year end. Such variations could have a material impact on the financial statements. For 2018/19, the impact of Brexit may increase this volatility, particularly for investment and property valuations.

Overview of our 2018/19 audit strategy

Audit risks and areas of focus			
Valuation of Property Investments (Level 2 Fair Value hierarchy)	Inherent risk	New risk	The Pension Fund's investment valuations are classified into three levels, according to the quality and reliability of information used to determine fair value. As at 31 March 2018, Hampshire Pension Fund held a significant balance of level 2 investments. Assets at Level 2 are those where quoted market prices are not available; for example, where an instrument is traded in a market that is not considered to be active, or where valuation techniques are used to determine fair value. The Pension Fund held £491 million of these investments at 31st March 2018 of which £433 million relates to property investments. We consider the valuation of property investments to be of a higher degree of inherent risk because of the extent of estimation uncertainty. Management is required to make material judgemental inputs and apply estimation techniques, supported by a professional valuer, to arrive at the year value of property investments carried in the Net Assets Statement. Although we are now reporting this as a new inherent risk relevant to the 2018/19 audit our audit procedures relating to valuation of Property Investments are not expected to significantly change from the previous period.

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Materiality

Planning materiality £66.1m

Materiality has been set at £66,132,000, which represents 1.0% of the 2017/18 net assets.

Performance materiality £49.6m

Performance materiality has been set at £49.599,000, which represents 75% of materiality.

Audit differences £3.3m

We will report all uncorrected misstatements relating to the Net Assets Statement and Pension Fund Account greater than £3,307,000. Other misstatements identified will be communicated to the extent that they merit the attention of the Audit Committee.

Overview of our 2018/19 audit strategy

Audit scope

This Audit Plan covers the work that we plan to perform to provide you with:

- Our audit opinion on whether the financial statements of Hampshire Pension Fund give a true and fair view of the financial position as at 31 March 2019 and of the income and expenditure for the year then ended; and

- Our conclusion on the Pension Fund's arrangements to secure economy, efficiency and effectiveness.

Our audit will also include the mandatory procedures that we are required to perform in accordance with applicable laws and auditing standards.

When planning the audit we take into account several key inputs:

- Strategic, operational and financial risks relevant to the financial statements;
- Developments in financial reporting and auditing standards;
- The quality of systems and processes;
- Changes in the business and regulatory environment; and,
- Management's views on all of the above.

By considering these inputs, our audit is focused on the areas that matter and our feedback is more likely to be relevant to the Pension Fund.

We will provide an update to the Audit Committee on the results of our work in these areas in our report to those charged with governance scheduled for delivery in July 2018.

02 Audit risks

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Misstatements due to fraud or error*

Financial statement impact

Misstatements that occur in relation to the risk of fraud due to management override could affect a number of areas of the financial statements.

What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As identified in ISA (UK) 240, management is in a unique position to perpetrate fraud because of its ability to manipulate accounting records directly or indirectly and prepare fraudulent financial statements by overriding controls that otherwise appear to be operating effectively. We identify and respond to this fraud risk on every audit engagement.

What will we do?

We will undertake our standard procedures to address fraud risk, which include:

- Inquiry of management about risks of fraud and the controls put in place to address those risks.
- Understanding the oversight given by those charged with governance of management's processes over fraud.
- Consideration of the effectiveness of management's controls designed to address the risk of fraud.

Performing mandatory procedures regardless of specifically identified fraud risks, including:

- Testing the appropriateness of journal entries recorded in the general ledger and other adjustments made in the preparation of the financial statements.
- Assessing accounting estimates for evidence of management bias.
- Evaluating the business rationale for significant unusual transactions.

We will utilise our data analytics capabilities to assist with our work.

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Risk of manipulation of investment valuation*

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Financial statement impact

At a Pension Fund, we have assessed that the risk of misstatement of investment valuation through management override of controls as the most likely areas of manipulation, and that this would occur specifically through journal postings. The relevant accounts have the following balances in the 2017/18 financial statements:

Change in market value of investments
£152 million
Total investment assets:
£6,432 million

What is the risk?

The financial statements as a whole are not free of material misstatements whether caused by fraud or error.

As noted above, under ISA 240, management is in a unique position to perpetrate fraud through the override of controls. We have considered the main areas where management may have the incentive and opportunity to do this.

At a Pension Fund, we have assessed that the risk of misstatement of investment valuation through management override of controls as the most likely areas of manipulation, and that this would occur specifically through journal postings.

What will we do?

Our approach will focus on:

- Reviewing reconciliations to the fund manager, custodian and valuer reports and investigating any reconciling differences; and
- Checking the reconciliation of holdings included in the Net Assets Statement back to the source reports.

Our response to significant risks

We have set out the significant risks (including fraud risks denoted by*) identified for the current year audit along with the rationale and expected audit approach. The risks identified below may change to reflect any significant findings or subsequent issues we identify during the audit.

Valuation of complex Investments (Level 3 Fair Value hierarchy)

Financial statement impact

As at 31 March 2018, Hampshire Pension Fund held a significant balance of level 3 investments. These included £291 million private equity investments and £206 million hedge funds.

These investments are more complex to value.

In the 2017/18 financial statements, the Pension Fund disclosed that the accuracy of these valuation techniques as between within 5% and 10% or within £39.4 million of the estimated value.

What is the risk?

Investments at Level 3 are those where at least one input that could have a significant effect on the asset's valuation is not based on observable market data.

Significant judgements are made by the Investment Managers or administrators to value these investments whose prices are not publically available. The material nature of Investments means that any error in judgement could result in a material valuation error.

Market volatility means such judgments can quickly become outdated, especially when there is a significant time period between the latest available audited information and the fund year end. Such variations could have a material impact on the financial statements.

For 2018/19, the impact of Brexit may increase this volatility, particularly for investment and property valuations.

What will we do?

Our approach will focus on:

- Reviewing the latest available audited accounts for the relevant funds and ensuring there are no matters arising that highlight weaknesses in the fund's valuation;
- Where the latest audited accounts are not as at 31st March 2019, performing analytical procedures and checking the valuation output for reasonableness against our own expectations; and
- Testing accounting entries have been correctly processed in the financial statements.

If necessary, our internal valuation specialists will support our work in this area.

Other areas of audit focus

We have identified other areas of the audit, that have not been classified as significant risks, but are still important when considering the risks of material misstatement to the financial statements and disclosures and therefore may be key audit matters we will include in our audit report.

What is the risk/area of focus?	What will we do?
Valuation of Property Investments (Level 2 Fair Value hierarchy) We consider the valuation of property investments to be of a higher degree of inherent risk because of the extent of estimation uncertainty. Management is required to make material judgemental inputs and apply estimation techniques, supported by a professional valuer, to arrive at the year value of property investments carried in the Net Assets Statement.	We will: • Consider the work performed by the Fund's valuer, including the adequacy of the scope of the work performed, their professional capabilities and the results of their work; • Review the key assumptions used by the valuer; and • Test accounting entries have been correctly processed in the financial statements.

03 Audit materiality

Materiality

Materiality

For planning purposes, materiality for 2018/19 has been set at £66.1 million. This represents 1.0% of the Pension Fund's prior year net assets. It will be reassessed throughout the audit process. For Hampshire Pension Fund, the Net Asset Statement, which discloses the value of the investments held by the scheme, is the most appropriate measure rather than the Fund Account. Assets are key, as they cover the liabilities of the fund and generate significant income. Use of net assets as the measure of materiality is EY standard practice for pension funds.

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Net Assets
£6,613m

Planning materiality
£66.1m

Performance materiality
£49.6m

Audit differences
£3.3m

We request that the Audit Committee confirm its understanding of, and agreement to, these materiality and reporting levels.

Key definitions

Planning materiality – the amount over which we anticipate misstatements would influence the economic decisions of a user of the financial statements.

Materiality for the Pension Fund has been based on 1.0% net assets. In the prior year we applied 2.0%. Materiality has been reduced following an internal review process for the use of materiality at Major Local Audits. There are a number of reasons for this decision, and these include:
- Pension funds have a high level of public interest by their nature;
- There are uncertainties in the markets which are expected to continue in this financial year end and beyond. Pension funds are exposed to these uncertainties through their investments; and
- Consistency with our audit approach to materiality in the financial services sector.

Performance materiality – the amount we use to determine the extent of our audit procedures. We have set performance materiality at £49.6 million which represents 75% of planning materiality. We apply 75% when it is not an initial audit and we have a sound understanding of the entity and past experience with the engagement indicates that a higher risk of misstatement is unlikely.

Audit difference threshold – we propose that misstatements identified below this threshold are deemed clearly trivial. We will report to you all uncorrected misstatements over this amount relating to the fund account and the net assets statement that have an effect on returns or that relate to expenditure.

Other uncorrected misstatements, such as reclassifications and misstatements in statements or disclosures, and corrected misstatements will be communicated to the extent that they merit the attention of the Audit Committee, or are important from a qualitative perspective.

04 Scope of our audit

Our Audit Process and Strategy

Objective and Scope of our Audit scoping

Under the Code of Audit Practice our principal objectives are to review and report on the Pension Fund's financial statements:

1. Financial statement audit

Our objective is:

- To form an opinion on the financial statements under International Standards on Auditing (UK).
- To form an opinion on the consistency of the pension fund financial statements within the pension fund annual report with the published financial statements of Hampshire County Council.

We also perform other procedures as required by auditing, ethical and independence standards, the Code and other regulations. We outline below the procedures we will undertake during the course of our audit.

Procedures required by standards

- Addressing the risk of fraud and error;
- Significant disclosures included in the financial statements;
- Entity-wide controls;
- Reading other information contained in the financial statements and reporting whether it is inconsistent with our understanding and the financial statements; and
- Auditor independence.

Our Audit Process and Strategy (continued)

Audit Process Overview

Our audit involves:

- Identifying and understanding the key processes and internal controls; and
- Substantive tests of detail of transactions and amounts.

For 2018/19 we plan to follow a substantive approach to the audit as we have concluded this is the most efficient way to obtain the level of audit assurance required to conclude that the financial statements are not materially misstated.

Analytics:

We will use our computer-based analytics tools to enable us to capture whole populations of your financial data, in particular journal entries. These tools:

- Help identify specific exceptions and anomalies which can then be subject to more traditional substantive audit tests; and
- Give greater likelihood of identifying errors than random sampling techniques.

We will report the findings from our process and analytics work, including any significant weaknesses or inefficiencies identified and recommendations for improvement, to management and the Audit Committee.

Internal audit:

We will regularly meet with the Head of Internal Audit, and review internal audit plans and the results of their work. We will reflect the findings from these reports, together with reports from any other work completed in the year, in our detailed audit plan, where they raise issues that could have an impact on the financial statements.

05 Audit team

Audit team

Audit team structure:

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Pension Specialist

EY Actuaries

Maria Grindley*
Associate Partner

Martin Young
Manager

Jack Dunkley
Assistant Manager

Maria Davison
Senior

Working together with the Pension Fund

We are working together with officers to identify continuing improvements in communication and processes for the 2018-19 audit.

We will continue to keep our audit approach under review to streamline it where possible.

* Key Audit Partner

Use of specialists

When auditing key judgements, we are often required to use the input and advice provided by specialists who have qualifications and expertise not possessed by the core audit team. The areas where specialists are expected to provide input for the current year audit are:

Area	Specialists
Pensions Valuation	Management Specialist - Aon Hewitt PwC (Consulting Actuary to the NAO) EY Specialist - EY Actuaries
Investment valuations (Level 2 and Level 3)	Management Specialist – Colliers (Property valuations) EY Specialist - EY valuation specialist (if necessary)

In accordance with Auditing Standards, we will evaluate each specialist's professional competence and objectivity, considering their qualifications, experience and available resources, together with the independence of the individuals performing the work.

We also consider the work performed by the specialist in light of our knowledge of the Pension Fund's business and processes and our assessment of audit risk in the particular area. For example, we would typically perform the following procedures:

- Analyse source data and make inquiries as to the procedures used by the specialist to establish whether the source data is relevant and reliable;
- Assess the reasonableness of the assumptions and methods used;
- Consider the appropriateness of the timing of when the specialist carried out the work; and
- Assess whether the substance of the specialist's findings are properly reflected in the financial statements.

06 Audit timeline

Audit timeline

Timetable of communication and deliverables

Timeline

Below is a timetable showing the key stages of the audit and the deliverables we have agreed to provide to you through the audit cycle in 2018/19

From time to time matters may arise that require immediate communication with the Audit Committee and we will discuss them with the Audit Committee Chair as appropriate. We will also provide updates on corporate governance and regulatory matters as necessary.

Audit phase	Timetable	Audit committee timetable	Deliverables
Planning: Risk assessment and setting of scopes.	November		
Walkthrough of key systems and processes	November - December		
Testing of routine processes and controls	February	Audit Committee	Audit Planning Report
Testing of routine processes and controls	March		
Year end audit Audit Completion procedures	June / July	Audit Committee	Audit Results Report Audit opinions and completion certificates
Year end audit Audit Completion procedures	July / August	Audit Committee	Annual Audit Letter

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07 Independence

Introduction

The FRC Ethical Standard and ISA (UK) 260 “Communication of audit matters with those charged with governance”, requires us to communicate with you on a timely basis on all significant facts and matters that bear upon our integrity, objectivity and independence. The Ethical Standard, as revised in June 2016, requires that we communicate formally both at the planning stage and at the conclusion of the audit, as well as during the course of the audit if appropriate. The aim of these communications is to ensure full and fair disclosure by us to those charged with your governance on matters in which you have an interest.

Required communications	
Planning stage	**Final stage**
▸ The principal threats, if any, to objectivity and independence identified by Ernst & Young (EY) including consideration of all relationships between the you, your affiliates and directors and us; ▸ The safeguards adopted and the reasons why they are considered to be effective, including any Engagement Quality review; ▸ The overall assessment of threats and safeguards; ▸ Information about the general policies and process within EY to maintain objectivity and independence. ▸ Where EY has determined it is appropriate to apply more restrictive independence rules than permitted under the Ethical Standard [note: additional wording should be included in the communication reflecting the client specific situation]	▸ In order for you to assess the integrity, objectivity and independence of the firm and each covered person, we are required to provide a written disclosure of relationships (including the provision of non-audit services) that may bear on our integrity, objectivity and independence. This is required to have regard to relationships with the entity, its directors and senior management, its affiliates, and its connected parties and the threats to integrity or objectivity, including those that could compromise independence that these create. We are also required to disclose any safeguards that we have put in place and why they address such threats, together with any other information necessary to enable our objectivity and independence to be assessed; ▸ Details of non-audit services provided and the fees charged in relation thereto; ▸ Written confirmation that the firm and each covered person is independent and, if applicable, that any non-EY firms used in the group audit or external experts used have confirmed their independence to us; ▸ Written confirmation that all covered persons are independent; ▸ Details of any inconsistencies between FRC Ethical Standard and your policy for the supply of non-audit services by EY and any apparent breach of that policy; ▸ Details of any contingent fee arrangements for non-audit services provided by us or our network firms; and ▸ An opportunity to discuss auditor independence issues.

In addition, during the course of the audit, we are required to communicate with you whenever any significant judgements are made about threats to objectivity and independence and the appropriateness of safeguards put in place, for example, when accepting an engagement to provide non-audit services.

We also provide information on any contingent fee arrangements , the amounts of any future services that have been contracted, and details of any written proposal to provide non-audit services that has been submitted;

We ensure that the total amount of fees that EY and our network firms have charged to you and your affiliates for the provision of services during the reporting period, analysed in appropriate categories, are disclosed.

Relationships, services and related threats and safeguards

We highlight the following significant facts and matters that may be reasonably considered to bear upon our objectivity and independence, including the principal threats, if any. We have adopted the safeguards noted below to mitigate these threats along with the reasons why they are considered to be effective. However we will only perform non –audit services if the service has been pre-approved in accordance with your policy.

Overall Assessment

Overall, we consider that the safeguards that have been adopted appropriately mitigate the principal threats identified and we therefore confirm that EY is independent and the objectivity and independence of Maria Grindley your audit engagement partner, and the audit engagement team have not been compromised.

Self interest threats

A self interest threat arises when EY has financial or other interests in the Pension Fund. Examples include where we receive significant fees in respect of non-audit services; where we need to recover long outstanding fees; or where we enter into a business relationship with you. At the time of writing, there are no long outstanding fees.

We believe that it is appropriate for us to undertake permissible non-audit services and we will comply with the policies that you have approved. At the time of writing, there are no non-audit fees associated with Hampshire Pension Fund. No additional safeguards are required.

A self interest threat may also arise if members of our audit engagement team have objectives or are rewarded in relation to sales of non-audit services to you. We confirm that no member of our audit engagement team, including those from other service lines, has objectives or is rewarded in relation to sales to you, in compliance with Ethical Standard part 4.

There are no other self interest threats at the date of this report.

Self review threats

Self review threats arise when the results of a non-audit service performed by EY or others within the EY network are reflected in the amounts included or disclosed in the financial statements.

There are no self review threats at the date of this report.

Management threats

Partners and employees of EY are prohibited from taking decisions on behalf of management of the Pension Fund. Management threats may also arise during the provision of a non-audit service in relation to which management is required to make judgements or decision based on that work.

There are no management threats at the date of this report.

Relationships, services and related threats and safeguards

Other threats
Other threats, such as advocacy, familiarity or intimidation, may arise. There are no other threats at the date of this report.

Other communications

EY Transparency Report 2018
Ernst & Young (EY) has policies and procedures that instil professional values as part of firm culture and ensure that the highest standards of objectivity, independence and integrity are maintained. Details of the key policies and processes in place within EY for maintaining objectivity and independence can be found in our annual Transparency Report which the firm is required to publish by law. The most recent version of this Report is for the year ended 1 July 2018 and can be found here: https://www.ey.com/uk/en/about-us/ey-uk-transparency-report-2018

08 Appendices

Appendix A

Fees

Public Sector Audit Appointments Ltd (PSAA) has published the fee scale for the audit of the 2018/19 accounts of opted-in principal local government and police bodies.

This is defined as the fee required by auditors to meet statutory responsibilities under the Local Audit and Accountability Act 2014 in accordance with the requirements of the NAO code.

	Planned fee 2018/19	Final Fee 2017/18
	£	£
Total Fee – Code work	24,442*	31,743
Total audit	24,442*	31,743

All fees exclude VAT

*PSAA has set the 2018/19 fee scale on the basis that individual scale audit fees for all opted-in bodies have been reduced by 23 per cent from the fees applicable for 2017/18. This gives opted-in bodies the benefit of the cost savings achieved in the recent audit procurement,

The agreed fee presented is based on the following assumptions:

► Officers meet the agreed timetable of deliverables;

► Our accounts opinion is unqualified;

► Appropriate quality of documentation is provided by the Pension Fund; and

► The Pension Fund has an effective control environment.

If any of the above assumptions prove to be unfounded, we will seek a variation to the agreed fee. This will be discussed with the Pension Fund in advance.

Fees for the auditor’s consideration of correspondence from the public and formal objections will be charged in addition to the scale fee.

Required communications with the Audit Committee

We have detailed the communications that we must provide to the Audit Committee.

Required communications	What is reported?	Our Reporting to you: When and where
Terms of engagement	Confirmation by the Audit Committee of acceptance of terms of engagement as written in the engagement letter signed by both parties.	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Our responsibilities	Reminder of our responsibilities as set out in the engagement letter	The statement of responsibilities serves as the formal terms of engagement between the PSAA's appointed auditors and audited bodies.
Planning and audit approach	Communication of the planned scope and timing of the audit, any limitations and the significant risks identified.	Audit planning report
Significant findings from the audit	• Our view about the significant qualitative aspects of accounting practices including accounting policies, accounting estimates and financial statement disclosures • Significant difficulties, if any, encountered during the audit • Significant matters, if any, arising from the audit that were discussed with management • Written representations that we are seeking • Expected modifications to the audit report • Other matters if any, significant to the oversight of the financial reporting process	Audit results report

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	What is reported?	When and where
Going concern	Events or conditions identified that may cast significant doubt on the entity's ability to continue as a going concern, including: • Whether the events or conditions constitute a material uncertainty • Whether the use of the going concern assumption is appropriate in the preparation and presentation of the financial statements • The adequacy of related disclosures in the financial statements	Audit results report
Misstatements	• Uncorrected misstatements and their effect on our audit opinion, unless prohibited by law or regulation • The effect of uncorrected misstatements related to prior periods • A request that any uncorrected misstatement be corrected • Corrected misstatements that are significant • Material misstatements corrected by management	Audit results report
Fraud	• Enquiries of the Audit Committee to determine whether they have knowledge of any actual, suspected or alleged fraud affecting the entity • Any fraud that we have identified or information we have obtained that indicates that a fraud may exist • A discussion of any other matters related to fraud	Audit results report
Related parties	Significant matters arising during the audit in connection with the entity's related parties including, when applicable: • Non-disclosure by management • Inappropriate authorisation and approval of transactions • Disagreement over disclosures • Non-compliance with laws and regulations • Difficulty in identifying the party that ultimately controls the entity	Audit results report

Appendix B

Required communications with the Audit Committee (continued)

		Our Reporting to you
Required communications	What is reported?	When and where
Independence	Communication of all significant facts and matters that bear on EY's, and all individuals involved in the audit, objectivity and independence Communication of key elements of the audit engagement partner's consideration of independence and objectivity such as: • The principal threats • Safeguards adopted and their effectiveness • An overall assessment of threats and safeguards • Information about the general policies and process within the firm to maintain objectivity and independence	Audit Planning Report Audit Results Report
External confirmations	• Management's refusal for us to request confirmations • Inability to obtain relevant and reliable audit evidence from other procedures	Audit results report
Consideration of laws and regulations	• Audit findings regarding non-compliance where the non-compliance is material and believed to be intentional. This communication is subject to compliance with legislation on tipping off • Enquiry of the Audit Committee into possible instances of non-compliance with laws and regulations that may have a material effect on the financial statements and that the Audit Committee may be aware of	Audit results report
Internal controls	• Significant deficiencies in internal controls identified during the audit	Audit results report
Representations	Written representations we are requesting from management and/or those charged with governance	Audit results report
Material inconsistencies and misstatements	Material inconsistencies or misstatements of fact identified in other information which management has refused to revise	Audit results report
Auditors report	• Any circumstances identified that affect the form and content of our auditor's report	Audit results report
Fee Reporting	• Breakdown of fee information when the audit plan is agreed • Breakdown of fee information at the completion of the audit	Audit planning report Audit results report

Appendix C

Additional audit information

Other required procedures during the course of the audit

In addition to the key areas of audit focus outlined in section 2, we have to perform other procedures as required by auditing, ethical and independence standards and other regulations. We outline the procedures below that we will undertake during the course of our audit.

Our responsibilities required by auditing standards	• Identifying and assessing the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. • Obtaining an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. • Evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management. • Concluding on the appropriateness of management's use of the going concern basis of accounting. • Evaluating the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation. • Obtaining sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Fund to express an opinion on the consolidated financial statements. Reading other information contained in the financial statements, including the board's statement that the annual report is fair, balanced and understandable, the Audit Committee reporting appropriately addresses matters communicated by us to the Audit Committee and reporting whether it is materially inconsistent with our understanding and the financial statements; and • Maintaining auditor independence.

Additional audit information (continued)

Purpose and evaluation of materiality

For the purposes of determining whether the accounts are free from material error, we define materiality as the magnitude of an omission or misstatement that, individually or in the aggregate, in light of the surrounding circumstances, could reasonably be expected to influence the economic decisions of the users of the financial statements. Our evaluation of it requires professional judgement and necessarily takes into account qualitative as well as quantitative considerations implicit in the definition. We would be happy to discuss with you your expectations regarding our detection of misstatements in the financial statements.

Materiality determines:

- The locations at which we conduct audit procedures to support the opinion given on the financial statements; and
- The level of work performed on individual account balances and financial statement disclosures.

The amount we consider material at the end of the audit may differ from our initial determination. At this stage, however, it is not feasible to anticipate all of the circumstances that may ultimately influence our judgement about materiality. At the end of the audit we will form our final opinion by reference to all matters that could be significant to users of the accounts, including the total effect of the audit misstatements we identify, and our evaluation of materiality at that date.

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HAMPSHIRE COUNTY COUNCIL

Decision Report

Decision Maker:	Audit Committee
Date:	21 February 2019
Title:	Minutes of the Hampshire Pension Fund Panel and Board Meeting – 15 November 2018
Report From:	Director of Transformation and Governance – Corporate Services

Contact name: Emma Clarke

Tel: 01962 847356 **Email:** emma.clarke@hants.gov.uk

1. Recommendation

1.1 That the Audit Committee receives and notes the minutes of the Hampshire Pension Fund Panel and Board meeting held on 15 November 2018 (attached at Appendix 1).

CORPORATE OR LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	yes
People in Hampshire live safe, healthy and independent lives:	yes
People in Hampshire enjoy a rich and diverse environment:	yes
People in Hampshire enjoy being part of strong, inclusive communities:	yes

Section 100 D - Local Government Act 1972 - background documents

The following documents discuss facts or matters on which this report, or an important part of it, is based and have been relied upon to a material extent in the preparation of this report. (NB: the list excludes published works and any documents which disclose exempt or confidential information as defined in the Act.)

Document	Location
None	

IMPACT ASSESSMENTS:

1. Equality Duty

1.1. The County Council has a duty under Section 149 of the Equality Act 2010 ('the Act') to have due regard in the exercise of its functions to the need to:

- Eliminate discrimination, harassment and victimisation and any other conduct prohibited under the Act;
- Advance equality of opportunity between persons who share a relevant protected characteristic (age, disability, gender reassignment, pregnancy and maternity, race, religion or belief, gender and sexual orientation) and those who do not share it;
- Foster good relations between persons who share a relevant protected characteristic and persons who do not share it.

Due regard in this context involves having due regard in particular to:

a) The need to remove or minimise disadvantages suffered by persons sharing a relevant characteristic connected to that characteristic;

b) Take steps to meet the needs of persons sharing a relevant protected characteristic different from the needs of persons who do not share it;

c) Encourage persons sharing a relevant protected characteristic to participate in public life or in any other activity which participation by such persons is disproportionally low.

1.2. **Equalities Impact Assessment:**

A high level Equalities Impact Assessment has been undertaken. The grants are intended to have a positive impact and advance equality.

2. Impact on Crime and Disorder:

2.1 Not applicable.

3. Climate Change:

a) How does what is being proposed impact on our carbon footprint / energy consumption?

Not applicable.

b) How does what is being proposed consider the need to adapt to climate change, and be resilient to its longer term impacts?

Not applicable.

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AT A MEETING of the Hampshire Pension Fund Panel and Board of HAMPSHIRE COUNTY COUNCIL held at Mitchell Room, EII Podium, Winchester on Thursday, 15th November, 2018

Chairman:
a Councillor M. Kemp-Gee

Elected members of the Administering Authority (Councillors):

p C. Carter
p A. Dowden
p A. Gibson
p J. Glen
p D. Mellor
p A. Joy
p P. Latham
p B. Tennent
p T. Thacker (Vice-Chairman)

Employer Representatives (Co-opted members):
a Councillor M. Chaloner (Southampton City Council)
a Councillor J. Smith (Portsmouth City Council)
p Councillor T. Cartwright (Fareham Borough Council)
p Mr D. Robbins (Churchers College)

Scheme Member Representatives (Co-opted members):
p Dr C. Allen (pensioners' representative)
p Mr N. Wood (scheme members representative)
p Mrs V. Arrowsmith (deferred members' representative)
p Mrs S. Manchester (substitute scheme member representative)

Independent Adviser:
p C. Dobson

BROADCASTING ANNOUNCEMENT

The Chairman announced that the press and members of the public were permitted to film and broadcast the meeting. Those remaining at the meeting were consenting to being filmed and recorded, and to the possible use of those images and recording for broadcasting purposes.

118. **APOLOGIES FOR ABSENCE**

Councillors Kemp-Gee and Smith sent their apologies.

119. **DECLARATIONS OF INTEREST**

Members were mindful that where they believed they had a Disclosable Pecuniary Interest in any matter considered at the meeting they must declare that interest at the time of the relevant debate and, having regard to the circumstances described in Part 3, Paragraph 1.5 of the County Council's Members' Code of Conduct, leave the meeting while the matter was discussed, save for exercising any right to speak in accordance with Paragraph 1.6 of the Code. Furthermore Members were mindful that where they believed they had a Non-Pecuniary interest in a matter being considered at the meeting they considered whether such interest should be declared, and having regard to Part 5, Paragraph 2 of the Code, considered whether it was appropriate to leave the meeting whilst the matter was discussed, save for exercising any right to speak in accordance with the Code.

120. **CONFIRMATION OF MINUTES (NON-EXEMPT)**

The minutes of the Pension Fund Panel and Board held on 28 September 2018 were confirmed.

121. **CHAIRMAN'S ANNOUNCEMENTS**

The Vice-Chairman welcomed Cllr Cartwright to his first meeting and updated the committee that the Panel and Board's Environmental, Social and Governance (ESG) working group would shortly be meeting for a third time before reporting back to the committee's December meeting.

Cllr Tennent fed back to the Panel and Board having attended the investment manager Schroders' trustee training event.

122. **ACCESS JOINT GOVERNANCE COMMITTEE MINUTES - 11 JUNE 2018**

The minutes of the ACCESS Joint Committee meeting (item 5 in the Minute Book) held on 11 June 2018 were noted.

123. **GOVERNANCE - FUNDING STRATEGY STATEMENT AMENDMENT FOLLOW-UP**

The Panel considered a report of the Director of Corporate Resources (item 6 in the Minute Book) following consultation on the changes to the Funding Strategy Statement (FSS) and Employer Policy in relation to the payment of exit credits following changes to the LGPS (Amendment) Regulations 2018 which were made in May 2018.

A consultation response was received from one employer and as a result revisions have been made to the wording of paragraph 12.7 of the Employer Policy which makes the agreement of a likely payment date part of the process for each exit rather than having a default policy in place. The Fund Actuary has recommended that a caveat is added alongside this change which will allow them to use more prudent assumptions if there is no agreement from an employer to accept a later payment date, even where the employer is late in providing the required information. The wording in paragraph 12.9 has also been altered slightly to make it clearer that it is only in very specific and limited circumstances that the Fund will not pay an exit credit to an exiting employer.

RESOLVED:

That the changes to the Funding Strategy Statement and Employer Policy were approved.

124. **EXCLUSION OF THE PRESS AND PUBLIC**

RESOLVED:

That the public be excluded from the meeting during the following items of business, as it is likely, in view of the nature of the business to be transacted or the nature of the proceedings, that if members of the public were present during these items there would be disclosure to them of exempt information within Paragraphs 3 of Part 1 of Schedule 12A to the Local Government Act 1972, and further that in all the circumstances of the case, the public interest in maintaining the exemption outweighs the public interest in disclosing the information, for the reasons set out in the reports.

125. **CONFIRMATION OF THE EXEMPT MINUTES OF THE PREVIOUS MEETING**

The exempt minutes of the Pension Fund Panel and Board held on 28 September 2018 were confirmed.

126. **INVESTMENT - INVESTMENT UPDATE**

The Panel and Board received an exempt report from the Director of Corporate Resources (Item 9 in the Minute Book) updating the Panel and Board on the Fund's investments [SUMMARY OF A MINUTE WHICH CONTAINS EXEMPT INFORMATION]

Chairman,

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By virtue of paragraph(s) 3, 5 of Part 1 of Schedule 12A of the Local Government Act 1972.

Document is Restricted

By virtue of paragraph(s) 3, 5 of Part 1 of Schedule 12A
of the Local Government Act 1972.

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