NORTH
OF TYNE
COMBINED
AUTHORITY

Cabinet

Tuesday, 12 March 2019 at 2.00 pm

Meeting to be held: Committee Room, North Tyneside Council, Quadrant, The Silverlink North, Cobalt Business Park, North Tyneside, NE27 0BY

www.northoftyne-ca.gov.uk

SUPPLEMENTAL AGENDA

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NORTH OF TYNE COMBINED AUTHORITY

Cabinet

12 March 2019

Subject: **2019-2022 Financial Plan and Budget (including Appointment of External Auditor)**

Report by: **Janice Gillespie, Chief Finance Officer**

Report Summary

The purpose of this report is to approve the budget for the North of Tyne Combined Authority (NTCA) for 2019/20, and the medium term financial plan for the period 2019/20 to 2021/22. Cabinet is recommended to approve the budget.

As the Combined Authority was only established in November 2018 the budgets for both this financial year and financial year 2019/20 reflect a set up phase in which the organisation is both establishing capacity to undertake its new responsibilities and beginning to deliver its priorities.

In developing these budget proposals the interim Mayor and Cabinet have been clear that NTCA should be a lean, agile, outward-facing organisation, working closely with stakeholders to achieve its goals. The new combined authority will draw on the expertise of its three constituent authorities to maximise opportunities for efficiency, including through use of Service Level Agreements for key corporate functions. The authority will also look to maximise funding available through use of the £20m per annum Investment Fund to leverage in additional investment. There is no additional cost to local taxpayers or local authorities in the current proposals.

Recommendations

The Cabinet is recommended to:

1. Agree the Corporate Budget for 2019/20 as set out in Paragraph 1.1

2. Agree the Investment Fund Budget as set out in paragraph 1.4

3. Agree the Treasury Management Strategy 2019/20 as described in paragraph 1.6 and attached at Appendix A

4. Note that the Transport Levies were issued on the 15 February as required

5 Agree to hold the level of reserves set out in paragraph 1.9 and to note that the Chief Finance Officer continues to keep the level of reserves under review as the Authority develops and new information becomes available about the financial risks facing authority arrangements for managing those risks; and,

6. Agree the appointment of Ernst Young as the External Auditor for the financial years 2018/19 and 2019/20 (Paragraph 1.13)

1. Background Information, Proposals and Timetable for Implementation

1.1 Combined Authority Medium Term Financial Plan – Corporate Budget

On the 4 December the Combined Authority set a Corporate Budget for 2018/19 which established an initial baseline position.

Since that time officers have continued to consider the early requirements of the new authority and Table 1 below identifies the proposed core budget that is required to operate the Mayoral Combined Authority and how it is to be funded.

Table 1 Draft 2019/20 Budget and 2019-22 Financial Plan

	2019/20	2020/21	2021/22
Expenditure	£	£	£
Staffing	1,602,641	1,698,772	1,732,647
Mayor and office	169,704	188,835	192,611
Policy Development Capacity	305,000	5,000	5,000
Miscellaneous (includes Mayoral election 2019/20)	1,399,000	199,000	174,000
Service Level Agreements	197,270	201,215	176,799
Total Expenditure	**3,673,616**	**2,292,822**	**2,281,057**
Income			
Contributions from the constituent Authorities	(120,000)	(120,000)	(120,000)
Mayoral Capacity Fund	(1,000,000)	(750,000)	0
Investment Fund Contribution	(2,400,000)	(1,300,000)	(2,000,000)
AEB Income	(153,616)	(122,822)	(161,057)
Total Income	**(3,673,616)**	**(2,292,822)**	**(2,281,057)**
NET (Income)/Expenditure	0	0	0

In developing these budget proposals the Interim Mayor and Cabinet have been clear in their approach to ensuring the North of Tyne Authority is a lean organisation. The budget proposals include the anticipated capacity required to deliver the ambition of the authority, and will be regularly reviewed as the delivery of key priorities and actions progress. The bulk of expenditure is funded through devolved funding secured through the devolution deal, with no change in contributions from constituent authorities compared to previous arrangements. The Interim Mayor and Cabinet will be working with officers to maximise the opportunities of the three constituent authorities working together efficiently and effectively with the North of Tyne Combined Authority. Some of this is already in place through the development of the Service level Agreements for support services such as Human Resources and Legal Services from across the three constituent authorities. A further example of this is with regard to the approach to procurement and the opportunity to consider how best the Procurement Strategies across the constituent authorities can support the ambition and delivery of the Vision for North of Tyne.

1.2 Mayoral Election Costs

It is a requirement of Government that Mayoral Election costs need to be funded by the Combined Authority, although NTCA has also secured a £2M Mayoral Capacity Fund grant from Government to support set up costs including the election. The estimated costs relating to the delivery of the election is £1.20m. This includes promotion and publicity costs, including mandated statutory requirements. Officers across the three constituent authorities have worked together to minimise costs by reviewing existing local arrangements and maximising the opportunities of local elections happening at the same time.

1.3 Mayoral Allowance

Included in the Corporate Budget is provision for the Mayoral allowance which was agreed by Cabinet on 5 February.

1.4 Investment Fund Budget

The Investment fund sets out indicative early costs associated with the development of proposals to be delivered through the Investment fund. The late establishment of the Authority in 2018/19 has a direct impact on the timing of decisions to award funding support to projects and the level of expenditure in 2018/19 and through in to 2019/20.

At its meeting on 4 December Cabinet considered early investment priorities which include:

- Inspiring the development of STEM and Digital skills in young people
- Help Residents into work- Returnship project
- Attracting new business to the North of Tyne, and
- Enhancing Rural Business Growth

In addition, Cabinet identified projects for early business case development funding for, which include

- Local Fibre Network
- North Shields Town Centre Redevelopment /Fish Quay
- Energy Central Learning Hub Blyth
- Targeted employment support for areas of Newcastle with the Highest unemployment levels, and
- The Northumberland, Newcastle and North of Tyne rail line

Some of these proposals are being considered by Cabinet at this meeting today.

The proposed Investment Fund budget set out in Table 2 attempts to recognise the impact of timing on the ability to issue funding and projects to be in a position to deliver in 2019/20 and the impact through to 21/22. At this stage no assumptions have been made regarding match funding opportunities that may arise as the investment proposals are developed, but it is anticipated the fund will be used to maximise the opportunities to secure other funding across the North of Tyne area.

Cabinet will be updated on progress against the proposed budget and any revisions required as the year end is approached. Included in the budget is provision for Technical Support -this is a requirement of the Assurance Framework that Investment Fund proposals are subject to external independent testing. Any unspent Investment Fund will be held and transferred to a specific reserve at the year end to support the delivery of the programme of work in future years.

Table 2 Proposed 2019/20 Investment Fund Budget

	2019/20	2020/21	2021/22
Expenditure	£	£	£
Supporting Business Case development	750,000	750,000	750,000
Work streams	975,000	7,200,000	12,200,000
Technical Support	250,000	250,000	250,000
Contribution to Corporate Costs	2,400,000	1,300,000	2,000,000
Total Expenditure	**4,375,000**	**9,500,000**	**15,200,000**
Income			
Investment fund	(20,000,000)	(20,000,000)	(20,000,000)
Total Income	**(20,000,000)**	**(20,000,000)**	**(20,000,000)**
NET (Income)/Expenditure	**(15,625,000)**	**(10,500,000)**	**(4,800,000)**
Investment Reserve Brought forward	**(19,011,667)**	**(34,636,667)**	**(45,136,667)**
Net Investment Fund Reserve Carried Forward	**(34,636,667)**	**(45,136,667)**	**(49,936,667)**

As can be seem from Table 2 2019/20 will continue to be a year of development of plans for the delivery of the Vision and its priorities with the expectation that these plans will see more financial investment achieved beyond 2019/20.

1.5 Mayoral Precept

No provisions has been included in the Financial Plan for a Mayoral precept

1.6 Treasury Management Strategy

The Authority is required to approve a Treasury Management Strategy each year and this is attached at Appendix A for approval. Additional work will progress during 2019/20 to identify potential synergies from alignment of the Treasury Management Strategy of this Authority with those of the constituent authorities, and the outcome of this work will be brought back to Cabinet for their consideration in due course.

1.7 Prudential Indicators and MRP Policy

The new arrangements set out in the NECA and NTCA Orders require decisions about the Transport Revenue Budget and Levies and the Transport Capital Programme to be determined by the new Joint Transport Committee (JTC). The transport functions and assets still rest with each Combined Authority but can only be exercised or deployed through the decisions of the Joint Transport Committee.

As previously outlined to Cabinet a proportion of the outstanding balance of the loans and investments (based on the share of Tyne and Wear population in each combined authority areas) will be shown in the balance sheets of the two Combined Authorities. It may be necessary for the individual loan agreements with lenders to be amended to reflect the new arrangement for the share of liabilities between the two Combined Authorities. The Interim Mayor and Cabinet are required to be aware of the associated prudential indicators and MRP policy associated with the loans and Investments which are included in the budget report for the NECA as the relevant accountable body. There is no change to the details of these as in the report to Cabinet on 5 February. A summary of the Loans outstanding at the date of the change in governance is set out in Table 3 below.

Table 3: Transport (Tyne and Wear) Outstanding Debt, and Capital Financing Requirement at 2nd November 2018

	Principal	Interest Due	Total	NECA Share	NTCA Share
	£000	£000	£000	£000	£000
Capital Financing Requirement	**193,665**		**193,665**	**107,883**	**85,782**
Actual External Debt	**167,333**	**2,274**	**169,607**	**94,482**	**75,125**

The Prudential Indicators and MRP policy for the Transport Asset and liabilities and NECA Budget remain unchanged from the report to Cabinet on 5 February 2019.

At this early stage of the North of Tyne Combined Authority there is no borrowing requirement associated with the delivery of the Vision and priorities, therefore the Authority does not yet require its own Prudential Indicators or an MRP policy. These will be developed when necessary and brought back to Cabinet as part of the Budget and Financial Planning process in future years.

1.8 Transport Levy

Cabinet are aware that the North of Tyne and the North East Combined Authorities are required under the Transport Levying Bodies regulations to set the Revenue Budget and associated Transport Levies before 15 February 2019, in order to enable their constituent councils to take the levies and other contributions into account in setting their own budgets. The details of this requirement were noted by Cabinet on 5 February 2019 and the levies were issued as required on 15 February 2019.

1.9 Reserves

As set out in the Budget report to Cabinet on the 4 December 2018, a Corporate reserve of £200k was created. The level of reserve will remain under review as the Authority develops and new information becomes available about the financial risks facing NTCA and the arrangements in place for managing those risks.

1.10 Adult Education Budget

As part of the devolution deal the Combined Authority is working to progress the devolution of the Adult Education Budget. The Authority is currently developing a proposal to be considered by Central Government to agree the devolution of the Adult Education Budget (AEB), in most areas by 2020/21. AEB devolution will give the authority significant new powers and responsibilities in delivering both their mayoral priorities and the national skills agenda and priorities.
As part of the preparations for devolution of AEB, the Department for Education has made grant funding available for the preparation for the implementation of AEB. Funding is offered for staff costs and other operating costs. However, funding is not offered for costs that have already been incurred pre-November 2018, or costs which should be met by the authority such as existing members of staff who were in their devolution-related posts prior to November 2018.
At this stage a prudent estimate of the implementation grant has been included in the Corporate Budget Funding and an update will be provided to Cabinet once the award is confirmed. The full AEB budget will be reflected in the financial plan once the terms of the devolution for the provision of AEB have been agreed.

1.11 Overview and Scrutiny Committee

At the meeting of the Overview and Scrutiny on the 14 February 2019 consideration was given to the report on the Combined Authority's draft budget proposals for 2019/20 and the medium-term financial plan for the period 2019/2020 to 2021/22 which was set out in a report to Cabinet on 5 February 2019. The Committee asked for confirmation that quarterly financial management reports will be received by Cabinet, and that the Audit and Standards Committee will receive updates on the budget position through the receipt of the Statement of Accounts. The Committee also requested that officers ensure that training on Treasury Management was available for Cabinet, Overview and Scrutiny Committee and the Audit and Standards Committee. Officers agreed to take this recommendation forward as an action.

1.12 Pooling of Business Rates and 75% Business Rates Retention Pilot

The 3 constituent North of Tyne Authorities submitted an application to the Ministry of Housing, Communities and Local Government to be considered for a 75% Business Rates Retention Pilot Scheme in 2019/20.

In the Final Local Government Finance Settlement it was confirmed that the North of the Tyne's expression of interest to become a 75% Business Rate Retention Pilot was successful for 2019/20. The three constituent authorities will be part of a pooling arrangement for the North of the Tyne. A key feature of becoming a 75% business rates pilot is that Business Rate income above the current 49%/50% retention arrangements will be pooled across the pilot. The value of this additional income will be confirmed when the final NNDR3 return is completed for the pool during May 2020. At that time any additional growth secured will be available to the Combined Authority to further support the delivery of the Vision, working with the three constituent authorities.

1.13 External Audit Arrangements

The Local Audit and Accountability Act 2014 introduced a new requirement for all local authorities (including combined authorities) to procure and appoint their own external auditor (known as a 'local auditor') from 2017/18 onwards. As the North of Tyne Combined Authority was formally created on 2 November 2018, it is necessary to progress the appointment of a local auditor for the North of Tyne Combined Authority.

The appointment of a Local Auditor must comply with all relevant procurement laws, and the decision on the appointment must be made by Cabinet consulting and taking into account the advice of an independent Auditor Panel. The Auditor Panel, as approved by Cabinet on the 5 February, met on the 26 February to consider a proposal from Ernst Young (the current External Auditor for the three constituent authorities) and agreed to support the appointment of Ernst Young as the external auditor for the financial years 2018/19 and 2019/20. The report of the Auditor Panel is attached as Appendix B.

A procurement process will be carried out during 2019/20 to progress the appointment of the External Auditor for the period 2020/21 to 2022/23.

1.14 The LEP Accountable Body Arrangements

When the North of Tyne Combined Authority was established the 7 North East authorities agreed that the former NECA's accountable body responsibilities should be shared between the new NECA and NTCA. The intention is that the NTCA will take on the accountable body function for the North East LEP, while NECA will act as accountable body for the Joint Transport Committee. The North East Combined

Authority (NECA) is currently the accountable body for the North East LEP and will be at the time when decisions relating to the 2019/20 Budget must be taken. Necessarily, the NECA budget report will include information about the funds available to the North East LEP and its proposed budget for 2019/20, which will be agreed by the North East LEP Board. The budget will need to reflect decisions about the level of government grant available to support North East LEP costs as well as the guidance and resource requirements needed to meet grant conditions. A further report will be brought back to this Cabinet once the LEP have made their decision regarding the accountable body function.

2. Potential Impact on Objectives

The North of Tyne Combined Authority Vision document sets out the strategic objectives of the Authority, detailing the key priorities and the first steps in the journey around the six key pillars. The budget will enable the Authority to properly discharge its functions and assist in delivering the Authority's vision, policies and priorities.

3. Key Risks

There are no key risks identified at this time.

4. Financial and Other Resources Implications

The report sets out finance and other resource considerations in detail.

5. Legal Implications

The Authority is required to agree a balanced budget annually and to monitor that budget throughout the year. The Authority must also make provision for an adequate level of un-earmarked reserves. It is also required to ensure that good financial governance arrangements are in place.

All relevant authorities are required under the Local Audit and Accountability Act 2014 to appoint a local auditor. The Authority must also consult and take into account the advice of its auditor panel on the selection and appointment of the local auditor under section 7 of the same Act.

6. Consultation/Engagement

The creation of the North of Tyne Combined Authority has been subject to significant regional and national engagement. The 2019/20 Budget is based on the devolution deal and the statutory orderwhich created the Authority, and the Authority's Vision which has been agreed by Cabinet and is being shared with stakeholders in a range of events.

A Business Summit held on the 1 March 2019 included consultation on the draft budget and the Community and Voluntary Sector were consulted during February. No specific feedback has been received to date with regard to the proposed budget.

7. Appendices

Appendix A Treasury Management Strategy
Appendix B Report of the Independent Auditor Panel

8. Background Papers

8 November Cabinet Report: North Tyneside Combined Authority Vision and Emerging Priorities of Early Investment.
The Combined Authorities (Finance) Order 2017.
Statutory Instrument No 1133 (2018) The Newcastle Upon Tyne, North Tyneside and Northumberland Combined Authority (Establishment and Functions) Order 2018.
8 November Cabinet 2018/19 Budget Report
5 February Cabinet 2019/20 Budget Report

9. Contact Officers

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10. Sign-off

Head of Paid Service: X
Monitoring Officer: X
Section 73 Officer: X

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Appendix A

North of Tyne Combined Authority

Treasury Management Policy Statement & Strategy 2019/20

Background

The Authority is required to operate a balanced budget, which means that cash raised during the year will meet cash expenditure. A key part of the Authority's treasury management function is to ensure that cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Authority's low risk policy, providing adequate security and liquidity before considering investment return.

Another key element of the treasury management function is the management of the funding associated with the Authority's capital investment plans. These capital plans provide a guide to any borrowing needs of the Authority, essentially the longer term cash flow planning to ensure that the Authority can meet its capital spending obligations. This management of longer term cash may involve arranging long or short term loans, or using longer term cash flow surpluses. It is not anticipated the Authority will undertake any borrowing during 2019/20 other than in respect of the relevant share of the Joint Transport Committee liabilities.

The contribution the treasury management function makes to the Authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or on larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security and liquidity of the sums invested.

Statutory Requirements

The Authority has a legal obligation under the Local Government Act 2003 to have regard to the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice; the Chartered Institute of Public Finance and Accountancy's Prudential Code: Capital Finance in Local Authorities and the Ministry of Housing, Communities and Local Government (MHCLG) Statutory Guidance on Local Government Investments.

The CIPFA Treasury Management Code requires the Authority to approve a treasury management strategy before the start of each financial year.

In addition, the MHCLG guidance requires the Authority to approve an investment strategy before the start of each financial year.

The CIPFA Treasury Management Code and the Prudential Code are closely linked. The Authority is required to have regard to the Prudential Code when setting limits to the level of its affordable borrowing. The 2017 update to the Prudential Code drew together the reporting requirements of the Prudential Code and the Treasury Management Code resulting in the requirement for the Authority to produce a capital strategy that includes specific requirements in respect of debt and borrowing and treasury management. An investment strategy will be produced when the Authority has determined potential borrowing limits through dialogue with the Treasury.

Effective Treasury Management

The Authority will create and maintain, as the cornerstones for effective treasury management:

- A treasury management policy statement, stating the policies, objectives and approach to risk management of treasury management activities
- Suitable Treasury Management Practices (TMPs), setting out the manner in which the Authority will seek to achieve its policies and objectives and detail how it will manage and control treasury management activities.

Reporting

The following reports will be issued during the financial year for approval by Cabinet:

- An annual report on the Authority's treasury management strategy and plan to be pursued in the coming year. This will include an investment strategy and will be considered by Cabinet as part of the budget approval process.
- A mid-year review report. This will update members on the progress of the capital position, show amended prudential indicators where required and performance against the strategy.
- An annual report, after year end closure on the performance of the treasury management function, on the effects of decisions taken and the transactions executed in the past year, and any circumstances of non-compliance with the treasury management strategy and TMPs.

Responsibilities

The Authority delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet and for the execution and administration of treasury management decisions to the Chief Finance Officer, who will act in accordance with the organisation's policy statement and TMPs.

Responsibility for ensuring effective scrutiny of the treasury management strategy and policies is delegated to Overview and Scrutiny Committee.

The Authority's treasury management function is proposed to be managed under a service level agreement with North Tyneside Council.

The Treasury Management functions of the Joint Transport Committee are approved as part of the North East Combine Authority budget setting process in their role as Accountable Body. A review of the NECA Treasury Management Strategy has been undertaken and is in line with that of the Authority.

Training

The CIPFA Treasury Management Code requires the responsible officer to ensure those members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

Treasury Management Policy Statement 2019/20

The Authority defines its treasury management activities as:

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

Risk Management

The Authority regards the successful identification, monitoring and control of risk to the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage those risks.

Value For Money

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

Borrowing Policy

At this current time the Authority does not have the powers to borrow other than for Transport responsibilities, the borrowing that will be reflected in this Authority's statement of accounts relates to historic Tyne and Wear Transport activities and the financing and borrowing costs are met by the Tyne and Wear Levy. Details of which are included the Treasury Management Strategy and Prudential Indicators of the North East Combined Authority as the appointed accountable body.

Investment policy

The Authority's primary objectives for the investment of its surplus funds are to protect the principal sums invested from loss, and to ensure adequate liquidity so that funds are available for expenditure when needed. The generation of investment income to support the provision of the Authority's services is an important, but secondary, objective.

The Authority will have regard to the MHCLG Guidance on Local Government Investments and will approve an investment strategy each year as part of the treasury management strategy. The strategy will set criteria to determine suitable organisations with which cash may be invested, limits on the maximum duration of such investments and limits on the amount of cash that may be invested with any one organisation.

Treasury Management Strategy for 2019/20

The proposed strategy for 2019/20 in respect of the following aspects of the treasury management function is based upon the treasury management officers' view on interest rates, supplemented with market forecasts provided by to North Tyneside Council's treasury advisor, Link Asset Services. This strategy covers:

- Treasury management consultants
- The current treasury portfolio position;
- Prospects for interest rates;
- The borrowing strategy;
- Sources of borrowing
- Policy on borrowing in advance of need;
- The investment strategy;
- Financial investments;
- Creditworthiness;
- Liquidity management;
- Non-financial investments; and
- Policy on the use of financial derivatives

Treasury Management Consultants

Through a service level agreement with North Tyneside Council, the Authority uses Link Asset Services as its external treasury management advisors.

Whilst the Authority has external treasury management advisors it recognises that responsibility for treasury management decisions remains with the Authority at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, that from our treasury advisers.

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

Current Treasury Portfolio Position

This will be updated following the receipt of the £20m devolved funding to the authority

Prospects for Interest Rates

The Authority through its service level agreement with North Tyneside Council for treasury management services has access to Link Asset Services as its external treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. The table below sets out Link Asset Services professional view of interest rates.

Link Asset Services forecast interest rates – (1 January November 2018)

	Bank Rate %	5 year PWLB %	10 year PWLB %	25 year PWLB %	50 year PWLB %
Dec 2018	0.75	2.00	2.50	2.90	2.70
Mar 2019	0.75	2.10	2.50	2.90	2.70
Jun 2019	1.00	2.20	2.60	3.00	2.80
Sep 2019	1.00	2.20	2.60	3.10	2.90
Dec 2019	1.00	2.30	2.70	3.10	2.90
Mar 2020	1.25	2.30	2.80	3.20	3.00
Jun 2020	1.25	2.40	2.90	3.30	3.10
Sep 2020	1.25	2.50	2.90	3.30	3.10
Dec 2020	1.50	2.50	3.00	3.40	3.20
Mar 2021	1.50	2.60	3.10	3.40	3.20

From time to time, gilt yields, and therefore PWLB rates, can be subject to exceptional levels of volatility due to geo-political, sovereign debt crisis, emerging market developments and sharp changes in investor sentiment. Such volatility could occur at any time during the forecast period.

Economic and interest rate forecasting remains difficult with so many external influences weighing on the UK. The above forecasts, and MPC decisions, will be liable to further amendment depending on how economic data and developments in financial markets transpire over the next year. Geographical developments, especially in the EU, could also have a major impact. Forecasts for average investment earnings beyond the three-year time horizon will be dependent on economic and political developments.

Investment and Borrowing Rates

Investment returns are likely to remain low during 2019/20 but to be on a gently rising trend over the next few years;

Borrowing interest rates have been volatile so far in 2018/19 and have increased modestly since the summer. This increase is expected to continue over the next few years (see table above).

Borrowing Strategy

The Authority currently does not expect to borrow in 2019/20 other than for the Joint Transport Budget the requirements of which are set out in Appendix B to the 5 February Cabinet Report

Annual Investment Strategy

Investment policy

The Authority'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.

The Authority's investment strategy will give consideration to core balances and cash flow requirements and the outlook for short-term interest rates. Where cash flow identifies cash sums that could be invested for longer periods (potentially obtaining a greater return), the value to be obtained from longer term investments will be carefully assessed.

If it is thought that the Bank Rate is likely to rise significantly within the time horizon being considered, then consideration will be given to keeping most investments as being short term or variable. Conversely, if it is thought that Bank Rate is likely to fall within that time period, consideration will be given to locking in higher rates currently obtainable, for longer periods.

Both the CIPFA Treasury Management Code and MHCLG guidance require the Authority to invest any funds prudently and to have regard to the security and liquidity of its investments before seeking the highest rate of return or yield.

The above Code and guidance also emphasises the importance of the management of risk within treasury management functions. This Authority has adopted a prudent approach to managing risk and defines its risk appetite by the following means:-

- Minimum acceptable credit criteria are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short term and long term ratings.

- Credit ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. Any assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Authority will engage with its advisors to maintain a monitor on market pricing such as credit default swaps and overlay that information on top of the credit ratings.

- Other information sources used will include the financial press, share prices and other such information pertaining to the banking sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

- The Authority has defined a list of types of investment instruments that the treasury management function are authorised to use. There are two lists in under the categories of 'specified' and 'non-specified' investments.

Financial Investments

The CIPFA Treasury Management Code and the MHCLG guidance has now extended the meaning of 'financial investments' to include the following:

- Specified investments;
- Loans; and
- Non-specified investments.

Specified Investments

Specified investments are: denominated in sterling; repayable within 12 months (either because of an expiry date or through a non-conditional option); not defined as capital expenditure by legislation; and invested with a body or in an investment scheme described as high quality or invested with one of: the UK Government; a Local Authority; or a Parish Council or Community Council.

Loans

Loans could be to local enterprises, local charities, wholly owned companies and joint ventures as part of a wider strategy for local economic growth. In some cases these loans may not be seen as prudent if adopting a narrow definition of prioritising security and liquidity. To allow such loans to be made whilst continuing to have regard to the MHCLG guidance Local Authorities must be able to demonstrate in their strategy that:

- Total financial exposure to these types of loans is proportionate;

- That an allowed “expected credit loss” model for loans and receivables as set out in IFRS 9 Financial Instruments has been adopted to measure the credit risk of a portfolio;
- That appropriate credit control arrangements to recover overdue repayments is in place; and
- The Authority has formally agreed the total level of loans by type that it is willing to make and their total loan book is within their self-assessed limit.

Non-specified Financial Investments

Non-specified investments are any investment not meeting the definition of a specified investment (less high credit quality, may be for periods in excess of 12 months, and are more complex instruments which require greater consideration by members and officers before being authorised for use).

The following table provides a list of specified investment instruments that are authorised to be used by the Authority, subject to cash limits and time limits indicated:

	Credit Criteria	**Maximum Deposit**	**Maximum Period**
Debt Management Agency Deposit Facility	UK Government backed	£50m	Unlimited
UK Local Authorities	N/A	£10m each	1 year
UK Government Treasury Bills	UK Sovereign Rating	£10m	1 year
Term deposits with banks and building societies	Blue /Orange Red Green No Colour	£5m each	12 months 6 months 100 days Not for use
Certificate of Deposits with banks and building societies	Blue /Orange Red Green No Colour	£5m each	12 months 6 months 100 days Not for use
Money Market Funds	AAA	£5m each	Liquid
Local Authority Controlled companies in the NTCA area		£5m	5 years

The following table provides a list of non-specified investment instruments that are authorised to be used by the Authority, subject to the cash limits and time limits indicated:

	Credit Criteria	Maximum Deposit	Maximum Period
UK Local Authorities	N/A	£5m each	3 years

The Authority has determined that it will limit the maximum total exposure to non-specified investments as being 25%

Investments will only be placed with counterparties from countries with a specified minimum sovereign rating.

All investments will be denominated in sterling.

The Authority will pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

Creditworthiness Policy

The minimum credit ratings criteria the Authority use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but they may still be used. In these instances consideration will be given to the whole range of ratings available or other market information, to support their use.

The Authority also applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies; Fitch, Moody's and Standard & Poor's. Link Asset Services supplement the credit ratings of counterparties with the following overlays:

- Credit watches and credit outlooks from credit rating agencies;
- Credit Default Swap (CDS) spreads to provide early warning of likely changes in credit ratings
- Sovereign ratings to select counterparties from only the most creditworthy countries

This modelling approach combines credit ratings, credit watches and credit outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties and are used by the Authority to determine the suggested duration of investments.

This service uses a wider array of information other than just primary ratings and by using a risk weighted scoring system it does not give undue preponderance to one agency's ratings.

The Authority is alerted to changes to ratings of all three agencies through its use of the Link Asset Services creditworthiness service.

If a downgrade results in the counterparty no longer meeting the Authority's minimum criteria, its further use as a new investment will be withdrawn immediately.

In addition to the use of credit ratings the Authority will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website. Extreme market movements may result in downgrade of an institution or removal from the Authority's lending list. Sole reliance will not be placed on the use of this external service. In addition this Authority will also use market data and market information on any external support for banks to help support its decision making process.

As a result in the change in accounting standards for 2018/19 under IFRS 9, the Authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year.

Liquidity Management

Officers providing treasury management services to the Authority use purpose-built cash flow forecasting software to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a prudent basis to minimise the risk to the authority of being forced to borrow on unfavourable terms to meet its financial commitments.

UK Banks – Ring Fencing

The largest UK banks are required, by UK law, to separate core retail banking services from their investment and international banking activities by 1st January 2019. This is known as ring-fencing. Whilst smaller banks with less than £25bn in deposits are exempt, they can choose to opt up. Several banks are very close to the threshold already and so may come into scope in the future regardless.

Ring-fencing is a regulatory initiative created in response to the global financial crisis. It mandates the separation of retail and small and medium-sized enterprise (SME) deposits from investment banking, in order to improve the resilience and resolvability of banks by changing their structure. In general, simpler, activities offered from within a ring-fenced bank, (RFB), will be focused on lower risk, day to day core transactions, whilst more complex and riskier activities are required to be housed in a separate entity, a non ring-fenced bank, (NRFB). This is intended to ensure than an entity's core activities are not adversely affected by the acts or omissions of other members of its group.

While the structure of the banks included within this process may have changed, the fundamentals of credit assessment have not. The Authority will continue to assess the new formed entities in the same way that it does others and those with sufficiently high ratings, will be considered for investment purposes.

Non-Financial Investments

The MHCLG guidance defines an investment as all of the financial assets of a Local Authority as well as other non-financial assets that the organisation holds primarily or partially to generate a profit; for example, investment property portfolios. This may therefore include investments that are not managed as part of normal treasury management processes or under treasury management delegations. The definition of an investment also covers loans made by a local authority to one of its wholly-owned companies or associates, to a joint venture, or to a third party.

The Authority recognises that investment in other financial assets and property primarily for financial return, taken for non-treasury management purposes, requires careful investment management. Such activity includes loans supporting service outcomes, investments in subsidiaries, and investment property portfolios.

The Authority will ensure that all the organisation's investments are covered in the investment strategy and will set out, where relevant, the organisation's risk appetite and specific policies and arrangements for non-treasury investments. It will be recognised that the risk appetite for these activities may differ from that for treasury management.

The Authority will maintain a schedule setting out a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and the organisation's risk exposure.

Policy on the use of Financial Derivatives

Local Authorities generally have made use of financial derivatives embedded into loans and investments both to reduce interest rate risk and to reduce costs or increase income at the expense of greater risk. The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over Local Authorities powers to use standalone financial derivatives such as swaps, forwards, futures and options. However, the Authority's policy is not to currently use these instruments.

Appendix B

NORTH OF TYNE COMBINED AUTHORITY

Local Audit and Accountability Act 2014 – Selection and Appointment of a Local (External) Auditor

Report of the Independent Auditor Panel

to

North of Tyne Combined Authority

12 March 2019

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Introduction

The Local Audit and Accountability Act 2014 requires that local authorities must establish or appoint an Auditor Panel to exercise the functions conferred on Auditor Panels under that Act. The Auditor Panel undertakes a variety of functions, including:

- Advising those authorities which it has been convened to support on the **maintenance of an independent relationship with the local auditor** appointed to audit the authorities' accounts
- Advising the authorities on the **selection and appointment of a local auditor** to audit the accounts
- (where relevant) Advising the authorities on any proposals by the authorities to **enter into a liability limitation agreement** with the local auditor
- Any other duties and functions which the Secretary of State may from time to time impose on the Auditor Panel.

The Auditor Panel

Newcastle City Council, North Tyneside Council and Northumberland County Council are the 'constituent authorities' of the North of Tyne Combined Authority(NTCA). These constituent authorities together convened one Auditor Panel to serve the requirements of all three authorities when appointing a Local Auditor to those three Authorities in 2017.

NTCA was established by statutory order on 2 November 2018. On 5 February 2019, the NTCA Combined Authority's Cabinet agreed that the independent Auditor Panel which had been previously established to advise on the appointment of a Local Auditor to the constituent authorities was also approved to act as the independent Auditor Panel on behalf of the North of Tyne Combined Authority.

The Local Audit and Accountability Act 2014 requires that the Panel must consist of a majority of independent members (or wholly of independent members); and must be independently chaired.

The NTCA Auditor Panel consists of the following independent members, all of whom independently chair or are independent members of the North of Tyne constituent authorities' respective Audit Committees, and are thus experienced in matters of local government audit and governance:

- **Mr Hamish Moore**, nominated to the Auditor Panel by Newcastle City Council – Chair of the Auditor Panel
- **Mr Kevin Robinson**, nominated to the Auditor Panel by North Tyneside Council
- **Mr Anthony (Ben) Haywood Smith**, nominated to the Auditor Panel by Northumberland County Council

Responsibilities Regarding Selection and Appointment of a Local Auditor

The Local Audit and Accountability Act 2014 requires that all relevant Authorities in England and Wales must make arrangements to appoint a local (external) auditor to audit their accounts by 31 December in the preceding financial year.

It is each authority's responsibility to consult and take into account the advice of its Auditor Panel on the selection and appointment of local auditor. It is the responsibility of the Auditor Panel to advise the Authority on the selection and appointment of a local auditor.

A Local Auditor for the North of Tyne Combined Authority

A single source quotation from Ernst and Young LLP to undertake Local Auditor duties was invited by the North of Tyne Combined Authority Chief Finance Officer (Section 73 Officer) in February 2019. Ernst and Young LLP are the incumbent Local Auditor appointed to Newcastle City Council, North Tyneside Council and Northumberland County Council following evaluation by the independent Auditor Panel at these three Authorities in 2017.

The independent Auditor Panel met on 26 February 2019 to consider the Ernst and Young proposal put forward by the Section 73 Officer in respect of the North of Tyne Combined Authority.

The independent Auditor Panel noted that the North of Tyne Combined Authority had only recently been created on 2 November 2018. The independent Auditor Panel further noted that it would be pragmatic and expedient to appoint a Local Auditor to ensure that relevant audit requirements were complied with by the North of Tyne Combined Authority.

The Auditor Panel drew attention to the fact that only one proposal for provision of Local Audit services had been sought and was available for the review. The independent Auditor Panel sought assurance from the Monitoring Officer for North of Tyne Combined Authority that this complied with prevailing procurement laws and specifically the rules relating to the North of Tyne Combined Authority together. In addition the panel was provided with further details of the considerations of the Section 73 Officer in receiving a single source quotation and the provision of value for money of the proposal from Ernst Young.

Recommendation of Auditor Panel

Having considered the single source proposal invited by the North of Tyne Combined Authority from Ernst and Young LLP, **the Auditor Panel advises to the North of Tyne Combined Authority that:**

The Independent Audit Panel has reviewed the proposal to appoint EY for a period of 2 years as external Auditors for a maximum annual fee of £24,000 + VAT.

Given the circumstances of the need to appoint an external Auditor, to meet strict deadlines and optimise the relationship between NTCA and the constituent authorities along with the assurances over due processes provided by John Softly and Janice Gillespie the Audit Panel supports the proposal to appoint EY.

The Audit Panel wishes to formally note that when this Contract is subject to renewal, the Audit Panel expects to be informed and involved in an appropriate process as early as possible to ensure that best practice from a Governance perspective is visibly adopted.

May the Audit Panel recognise the work of the officers in regard to this matter.

Report Authors:

Mr Hamish Moore, Chair of Auditor Panel
Mr Kevin Robinson
Mr Anthony (Ben) Haywood Smith