HAMPSHIRE COUNTY COUNCIL

Decision Report

Decision Maker:	Cabinet County Council
Date:	18 June 2018 19 July 2018
Title:	2017/18 – End of Year Financial Report
Report From:	Director of Corporate Resources – Corporate Services

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1. Recommendations

RECOMMENDATIONS TO CABINET

It is recommended that Cabinet:

1.1 Approves the outturn position set out in Section 3.

1.2 Approves the transfer of £6.25m to the Insurance Reserve to increase the reserve in line with most recent actuarial review.

1.3 Approves the transfer of £0.5m to the Investment Risk Reserve.

1.4 Approves the allocation of £1.4m of the net corporate savings to enable the County Council to provide funding to undertake vital remedial work to the county's road network following the prolonged cold and wet period.

1.5 Approves the transfer of the balance of the net corporate savings of approaching £17m to the Grant Equalisation Reserve (GER).

1.6 Approves the increase of service capital programme cash limits for 2018/19 to reflect the carry forward of capital programme schemes and shares of capital receipts, as set out in Appendix 3.

1.7 **Recommends to County Council that**:

a) The report on the County Council's treasury management activities and prudential indicators set out in Appendix 2 be approved.

RECOMMENDATIONS TO COUNTY COUNCIL

This single report is used for both the Cabinet and County Council meetings, the recommendations below are the Cabinet recommendations to County Council and may therefore be changed following the actual Cabinet meeting.

County Council is recommended to approve:

a) The report on the County Council's treasury management activities and prudential indicators set out in Appendix 2.

2. Executive Summary

2.1 This report provides a summary of the 2017/18 final accounts. The draft statement of accounts was submitted for audit on the 31 May 2018 and will be reported to the Audit Committee in July, in conjunction with the External Audit report on the accounts.

2.2 Net service cash-limited expenditure was £10.4m lower than budgeted against an overall gross budget of approaching £1.9bn, a variance in the region of 0.5%. This position reflects the County Council's continuing successful financial strategy of early delivery of resources from proposals in advance of need which provides funding that can then be used to meet the costs of change, to cash flow the delivery of savings or to offset service pressures.

2.3 The position for each of the departments is summarised in the table below:

	Variance (Under) / Over Budget £'000
Adults' Health and Care	0
Children's Services - Non Schools	0
Economy, Transport and Environment	(4,982)
Policy and Resources	(5,451)
Total Departmental Expenditure	**(10,433)**

2.4 The position for Adults' Health and Care reflects sustained management activity during the year to control spend in the face of well publicised care pressures. In addition, the effective use of the Improved Better Care Fund (IBCF), the conclusion of the Transformation to 2017 (Tt2017) Programme and the early realisation of £0.7m of savings have all contributed to balancing the position at the end of the year.

2.5 The break even position in Children's Services equally reflects significant management activity which has seen work to limit, as far as possible, pressures in the Children Looked After (CLA) budget, that continue to grow due to increasing activity levels and higher average costs due to the type of care being provided and the availability of that care. This alongside the early delivery of resources, use of cost of change reserves and agreed corporate support (including an additional £7.2m allocated at the end of the year) has resulted in a balanced position.

2.6 The final outturn position for Economy, Transport and Environment (ETE) shows savings against the budget of almost £5.0m due to early delivery of resources and savings primarily in Highways Traffic and Transport of which £0.6m relates to the winter maintenance budget that will be spent in 2018/19 as part of a remedial programme required following the prolonged very cold and wet start to 2018.

2.7 Policy and Resources achieved a saving against budget of approaching £5.5m, mainly due to ongoing efficiency savings and the early achievement of 2019/20 savings.

2.8 The net savings within ETE and Policy and Resources have been set aside for use by the respective services to meet restructuring and investment costs associated with the Transformation to 2019 (Tt2019) Programme and beyond, in accordance with the current financial management policy and the Medium Term Financial Strategy (MTFS).

2.9 In addition within ETE it is specifically proposed to again reinvest available funding associated with the winter maintenance budget in highways maintenance to provide additional one-off resources to supplement existing maintenance programmes. This flexibility was approved in February by Cabinet and County Council.

2.10 Schools are facing increasing financial pressure relating to high needs and early years, both at an individual school level and within the overall schools' budget. In 2017/18 the overall position has been balanced through the use of the Dedicated Schools Grant (DSG) Reserve however, the balance was not sufficient to cover these pressures in full. As a consequence, the resulting DSG deficit of £4.5m will be covered as part of the allocation of school budgets in 2018/19 to achieve a balanced position.

2.11 Savings on non-cash limited budgets total £25.1m. This is mainly as a result of treasury management activity (including the achievement a return of more than 4% from higher yielding investments) and unused contingencies. Contingencies were in the main set aside in recognition of the increased risk in the budget due to ongoing pressures within social care, together with the fact that a further £98m was removed from the budget in 2017/18.

2.12 This report recommends that of these corporate savings £6.25m be added to the Insurance Reserve to increase the reserve in line with most recent actuarial review and £0.5m be added to the Investment Risk Reserve.

2.13 In addition, it is proposed that:

- £1.4m is allocated to provide funding to undertake vital remedial work to the county's road network following the prolonged cold and wet period. This additional investment, along with the £0.6m from the 2017/18 winter maintenance budget (as referred to above in paragraph 2.6) will complement the Government's one-off pothole grant funding of £3.0m in 2018/19 to provide a total sum of £5m for this purpose.
- The balance of approaching £17m is transferred to the Grant Equalisation Reserve (GER) bringing the unallocated amount in the reserve up to circa £29.4m, in preparation for any future draw required beyond 2020 as set out in the MTFS which is presented elsewhere on the Agenda for approval. More detail is set in the table in paragraph 3.52.

2.14 The report contains a small section on reserves and balances highlighting that in line with the MTFS, the level of reserves has risen as we prepare for planned draws in the period to 2019/20 and beyond.

2.15 The report also recommends approval of:

- The annual report on the operation of the treasury management strategy, for subsequent approval by the County Council.
- The County Council's end of year prudential indicators.

- A revised capital financing plan for 2018/19.

3. 2017/18 Revenue Outturn

Service Cash Limits

3.1 The table below summarises the net outturn position for each department compared to the final cash limit for the year. The figures exclude schools spending but include cost of change paid for during 2017/18:

	Variance (Under) / Over Budget £'000
Adults' Health and Care	0
Children's Services - Non Schools	0
Economy, Transport and Environment	(4,982)
Policy and Resources	(5,451)
Total Departmental Expenditure	**(10,433)**

3.2 The third quarter monitoring position indicated that most departments, with the exception of Children's Services, were anticipating that they would be able to manage the large-scale investment required to deliver their planned transformation activity and to meet service pressures through the use of cost of change and other reserves, along with agreed corporate funding.

3.3 Strong financial management has remained a key focus throughout the year to ensure that all departments stay within their cash limits, that no new revenue pressures are created and that they deliver the savings programmes that have been approved. Enhanced financial resilience monitoring, which looks not only at the regular financial reporting but also at potential pressures in the system and the early achievement of savings being delivered through transformation, has continued through periodic reports to the Corporate Management Team (CMT) and to Cabinet.

3.4 This focus has ensured that at the end of the year the final position is in line with expectations and that departments have delivered resources early, which will provide funding that can then be used to meet the costs of change and to cash flow the delivery of savings or offset service pressures.

3.5 For Children's Services, revised funding for growth in Children Looked After (CLA) numbers, and in turn the knock on impact for care leavers, was agreed in February and that, alongside continued management focus, has enabled the Department to deliver a balanced position at the end of the year.

3.6 Key issues across each of the departments are highlighted in the paragraphs below and whilst pressures within social care services remain the highest risk and most volatile area of the County Council's budget the impact of successive savings programmes along with other service pressures means that all departments are facing financial pressure at the present time.

Adults’ Health and Care

3.7 Adults’ Health and Care have successfully contained the well publicised care pressures and delivered a breakeven financial position in 2017/18. This has been achieved in part through consistent and wider application of a strengths based approach to assessing clients care needs alongside the utilisation of one off funding; made available through grants and the Improved Better Care Fund (IBCF).

3.8 However, these sources of funding will only mitigate the pressure in the short term. Looking further ahead this non-recurrent funding will cease and over the same period it is anticipated that further care provision pressures will arise from both increases in demand and complexity of clients’ needs and from care costs to ensure market stability. Together this provides a major budgetary challenge to the Department that will require close monitoring and corporate support in future years.

3.9 In addition to meeting existing demand and costs pressures the majority of the IBCF funding has been spent on initiatives that support long term change and transformation of services, including those that benefit Health and that provide stability within the care market. The full funding allocation of £17m, for 2017/18 was spent in year by the Department.

3.10 Although it had been agreed by Cabinet that £13.1m of the Adults Transformation to 2017 (Tt2017) savings could be delayed to 2018/19 this has not been required. Earlier in the year there was sufficient confidence to close the Tt2017 Programme on the basis that the required further savings were guaranteed in 2018/19. Further to this the outturn position reported now indicates that the Department have fully mitigated all of the £13.1m savings in 2017/18, one year ahead of schedule.

3.11 The achievement of Tt2017 coupled with the early realisation of £0.7m of the Transformation to 2019 (Tt2019) Programme has placed the Department in a far stronger position as we move into 2018/19 to support both the costs of the Tt2019 programme and to cash flow the delivery of their savings.

3.12 Public Health ended the year with a balanced position, after making a contribution to the ring-fenced reserve of £1.7m. This has been achieved through planned work to deliver efficiencies and innovation within existing services in advance of future reductions in funding, including holding vacancies in the Public Health team and making reductions in contractual and non-contractual spend. The 2017/18 closing balance of the Public Health Reserve is £7.8m and it is planned to utilise this reserve over the short term to provide investment for further initiatives to drive down recurring costs and to offset reductions in the grant that will occur prior to the savings being achieved.

Children’s Services

3.13 Children’s Services have seen the number of CLA, including Unaccompanied Asylum Seeking Children (UASC) continue to grow during 2017/18, well above the levels that were forecast. In addition, there are other increasing cost pressures, particularly in relation to care leavers and the cost of agency staff.

3.14 Nationally there is growing attention being focused on the pressures facing children's services and analysis by the Local Government Association (LGA) published in the summer last year highlighted that growing demand for support is leading to over spends in an increasing number of authorities.

3.15 The Department have applied strong focus to these pressures and the reported position is break even, reflecting the pro-active management of the services together with early delivery of savings, the use of the departmental reserves and agreed corporate support; including additional support of £7.2m approved in February as part of budget setting. However, these pressures continue to be areas of some concern in Children's Services and will be closely monitored throughout the current year.

3.16 Funding has been set aside within contingencies to provide for the projected growth in CLA numbers (and in turn the knock on impact for care leavers) in 2018/19 and beyond. It is now anticipated that a further increase in funding is required to meet the financial consequences of updated growth projections and more detail is contained in the MTFS presented elsewhere on this Agenda.

3.17 Other challenges faced by the Department relate to the short supply of qualified social workers, an increase in the numbers of care leavers and the costs associated with the provision of school transport, mainly relating to those with special educational needs.

3.18 Further corporate support has been agreed to help alleviate the pressures being felt in these areas as part of the previous MTFS in October 2017, including funding to cover costs to grow social worker capacity through increased recruitment and improved retention. These amounts, together with the revised funding for growth in CLA numbers (and in turn the knock on impact for care leavers) set out in the updated MTFS presented elsewhere on this Agenda, alongside continued management focus on the other pressure areas, will help the Department to operate from a firmer financial base as work on the challenging transformation programme progresses.

Economy, Transport and Environment

3.19 The final outturn position for Economy, Transport and Environment (ETE) shows a saving against the budget of almost £5.0m due to early delivery of 2019/20 savings totalling £1.25m together with more than £3.7m of net savings on planned departmental activity. Included within this result is an amount of £0.6m within the winter maintenance budget.

3.20 At their meeting on 5 February 2018 Cabinet agreed to transfer any one off resources available within the 2017/18 winter maintenance budget to the highways maintenance budget for 2018/19. The highways maintenance budget will therefore be increased by £0.6m to reinvest in highways maintenance in 2018/19.

3.21 This additional investment, along with a recommended £1.4m to be allocated from the net corporate savings (as referred to in paragraphs 3.46 to 3.49) will complement the Government's pothole grant funding of £3.0m in 2018/19 to provide a total one-off sum of £5m for a programme of vital remedial work to the county's road network following the prolonged cold and wet period.

Policy and Resources

3.22 Policy and Resources achieved a saving against the budget of £5.5m, after substantial transformation costs have been met in year, mainly due to ongoing efficiency savings and the early achievement of 2019/20 savings.

3.23 The successful implementation of the Tt2019 Programme and the resulting early delivery of savings will be crucial as successive budget reductions mean there is less scope to generate savings across the services and high levels of investment and resources are required over a longer time period to generate further savings.

3.24 Detailed explanations for the outturn position for all departmental budgets are provided in Appendix 1.

3.25 The departmental savings will be set aside to meet the future cost of change in line with the current financial policy which incentivises good stewardship.

3.26 In addition within ETE the remaining resources associated with the 2017/18 winter maintenance budget will be set aside to provide additional one-off resources in 2018/19 as part of an additional £5m programme of highways maintenance.

Schools Budget

3.27 Financial pressures on schools are increasing, both at an individual school level and within the overall schools' budget. These pressures relate to both high needs and early years.

3.28 Pressures on the High Needs Block have mainly arisen due to significant increases in the number of pupils with additional needs. This is a pressure that is mirrored nationally and has been seen since the SEND reforms in 2017. There are also increases in the amount of funding being provided for each pupil on average due to increasing levels of need and these factors have created a pressure on the top-up budgets for mainstream schools, resourced provisions and further education colleges. There is also significant pressure due to more pupils requiring placements in independent and non-maintained schools.

3.29 There is a further pressure within the budget for early years due to an unexpected decline in the number of children recorded on the census.

3.30 In total for 2017/18 there was a net over spend of approaching £9.4m against the schools budget. Any year end over spend is usually met from the Dedicated Schools Grant (DSG) Reserve however the balance was not sufficient to cover these pressures in full. As a consequence, the resulting DSG deficit of £4.5m will be covered as part of the allocation of school budgets in 2018/19 to achieve a balanced position.

Other Budgets

3.31 The outturn for other items contained within in the budget is shown in the following table:

	Variance (Under) / Over Budget £m
Capital Financing / Interest on Balances	(7.0)
Waste Management	(4.3)
Contingencies	(12.6)
Other Net Variations	(1.2)
Total	**(25.1)**

3.32 The main reasons for these variances are set out in the paragraphs below.

Capital Financing and Interest on Balances (£7.0m Saving)

3.33 These savings reflect the ongoing trend of a very prudent approach to capital financing costs and interest on balances and the continuing use of 'internal borrowing' to fund capital expenditure rather than taking out long term loans at this point. In addition, a return of more than 4% from higher yielding investments has been achieved, in line with the approved Investment Strategy.

Waste Management (£4.3m Saving)

3.34 Due to the number of variables associated with the provision of the Waste Management contract, separate central provisions are made within the budget each year and released in line with changes in waste volumes or contract terms. Whilst waste volumes stabilised in previous years, requiring less to be drawn from contingencies, 2014/15 saw the first real increase in volumes for several years and the provision in future years was reviewed in light of this.

3.35 The upward trend in 2017/18 has been less than forecast resulting in savings against the budget, but continued close scrutiny of waste volumes will be required throughout 2018/19 to model and monitor the future costs.

Contingencies (£12.6m Saving)

3.36 The level of contingencies held as part of the 2017/18 budget reflected the well documented pressures and risk around demand and costs for the provision of social care services, together with the fact that a further £98m was removed from the budget in 2017/18. Through strong management, applied to manage demand and supress the additional costs, savings against these contingency amounts were realised.

3.37 Other contingencies which were not required in the year related to a central provision for carbon allowances and inflation / risk provisions (in particular for energy and business rates) which accounted for the balance of the overall saving within contingencies.

Other Net Variations (£1.2m Saving)

3.38 This relates to additional unanticipated Section 31 business rate relief grant income of £1.3m received in 2017/18, offset by a number of small variances.

Allocation of Net Saving

3.39 The net saving totals £25.1m and it is recommended that this amount is allocated as set out in paragraphs 3.40 to 3.53 below.

Insurance Reserve

3.40 The Council holds specific reserves to mitigate risks that it faces. The County Council self insures against certain types of risks and the level of the Insurance Reserve is based on an independent valuation of past claims experience and the level and nature of current outstanding claims.

3.41 Each year the County Council sets aside an insurance provision to meet claims resulting from incidents that have occurred during the year, along with reserves to cover potential claims arising from incidents in that year but where the claims are received in the future.

3.42 Regular actuarial reviews on the overall insurance fund have provided assurance that the County Council has been setting aside appropriate levels of funding against future liabilities to date. However, the conclusions of the most recent review are that there is a need to adopt a long term approach to increasing that fund going forward and the intention is to regularly review the Insurance Reserve and to make year end contributions that move the County Council towards the level outlined in the latest actuarial assessment.

3.43 To begin this it is proposed to add £6.25m to the Insurance Reserve which will result in a net increase of £5m after the provision for 2017/18 totalling £1.25m is set aside.

Investment Risk Reserve

3.44 The Investment Risk reserve was established in 2014/15 to mitigate the slight additional risk associated with the revised approved investment strategy as a prudent response to targeting investments with higher returns.

3.45 It is recommended that a further £0.5m is added to this reserve to further protect the County Council's funds. This is prudent given the additional risk that is being taken in targeting investments with higher returns and brings the total in the Investment Risk Reserve to £2m.

Highways Investment

3.46 It is recommended that £1.4m is allocated to be added to the budget for highways maintenance in 2018/19. This additional investment, along with the £0.6m from the 2017/18 winter maintenance budget (as referred to in paragraph 3.20) will complement the Government's one-off pothole grant funding of £3.0m in 2018/19 to provide a total sum of £5m for a programme of vital remedial work to the county's road network following the prolonged cold and wet period.

3.47 Hampshire experienced two severe winter events during February and March 2018 with widespread snowfall and localised travel disruption. Whilst both events were successfully managed and network operations restored relatively swiftly, the resulting damage to the highway network was extensive with the majority of roads suffering pothole and other structural damage. Immediately following the snow events a find-and-fix 'Pothole Busters' repair programme commenced and this has focussed on addressing the many thousands of new potholes that have developed with a combination of interim 'make safe' and also permanent repairs. Up to 12 'Hampshire Highways' teams continue to be deployed across the County undertaking localised pothole repairs and utilising handheld technology to accurately record the quantity, quality and extent of work that has been carried out. The 'Pothole Busters' initiative will continue for the remainder of 2018/19.

3.48 A more detailed network-wide assessment has since been completed and from this over 400 sites have been identified as having deteriorated as a direct consequence of the winter weather with an estimated cost of around £10m. A restoration plan is in the process of being formulated to target the worst of these with a combination of structural patching, full resurfacing and localised reconstruction. This larger package of work, which will utilise the additional funding, is expected to start in late May and will continue for the remainder of 2018/19 although the full restoration of the network to pre-2018 condition will require significant additional investment and is likely to take many years.

3.49 The additional funding will also be targeted at sites where there are known surface water flooding issues to ensure highway drainage systems remain fully functional in the lead up to the autumn and winter months when wetter weather can be expected.

Balance of Savings

3.50 It is proposed that the balance of the net savings of £17m be added to the Grant Equalisation Reserve (GER) bringing the unallocated amount in the reserve up to £29.4m, in preparation for any future draw required beyond 2020 as set out in the MTFS which is presented elsewhere on the Agenda for approval.

3.51 The current strategy that the County Council operates works on the basis of a two-year cycle of delivering departmental savings to close the anticipated budget gap, providing the time and capacity to properly deliver major savings programmes every two years with deficits in the intervening years being met from the GER. Building the provision within the GER will support the revenue position in future years, as set out in the MTFS, in order to give the County Council the time and capacity to implement the next phase of transformation to take us to 2021/22.

3.52 The table below summarises the forecast position for the GER before any requirement to balance the budget in 2020/21 or to provide corporate funding to cash flow the next stage of transformation which is likely, given the experience of Tt2019; although the scale is unknown at this stage:

	GER £'000
Balance at 31/03/2018	74,870
2018/19 Draw as per February Budget Setting	(26,435)
Further Budgeted Additions:	
MRP “Holiday”	21,000
Planned use:	
Cash Flow Tt2019	(40,000)
Unallocated Balance	**29,435**

3.53 Where possible, the County Council will continue to direct spare one off funding into this reserve as part of its overall longer term risk mitigation strategy, which has served it very well to date.

4. General Balances and Earmarked Reserves

4.1 The County Council’s reserves strategy, which is set out in the MTFS, is now well rehearsed and continues to be one of the key factors that underpin our ability not only to provide funding for the transformation of services but also to give the time for changes to be properly planned, developed and safely implemented.

4.2 We have made no secret of the fact that this deliberate strategy was expected to see reserves continue to increase during the period of tight financial control by the Government, although it was always recognised that the eventual planned use of the reserves would mean that a tipping point would come and we would expect to see reserves start to decline as they are put to the use in the way intended as part of the wider MTFS.

4.3 General Balances at the 31 March 2018 stand at £22.4m, and following the planned draw in 2018/19 this will reduce to be broadly in line with the current policy of carrying a general balance that is approximately 2.5% of the County Council’s Budget Requirement (currently a sum of circa £20m).

4.4 In addition to the general balance, the County Council maintains earmarked reserves for specific purposes and to a large extent the majority of these are committed either to existing revenue or capital programmes or to mitigate risks that the County Council faces through self insurance or funding changes by government.

4.5 In overall terms the total value of earmarked revenue reserves has increased as provision is built up in the GER, ahead of planned draws in line with the MTFS.

4.6 The net impact of the changes in the revenue account during 2017/18 mean that the GER will stand at almost £74.9m, which is in line with the financial strategy of supporting the revenue spend position as savings are developed and delivered on a two year cycle. Provision is being made for a draw in 2018/19 in order to give the County Council the time and capacity to implement the Tt2019 Programme and to cash flow the safe delivery of the programme so as we can complete the transformation to take us to 2019/20, and plan sensibly for future years.

4.7 In the period to 2021/22, the unallocated amount remaining in the reserve will be £29.4m, as shown in the table at paragraph 3.52. In preparation for any future draw required beyond 2020 further additions will be required to the GER as set out in the MTFS which is presented elsewhere on the Agenda for approval.

4.8 Other earmarked reserves will increase due to the timing of receipt of funds in advance of their planned use for an intended purpose, in particular in funding the capital programme. Schools balances, over which the County Council has no direct control, have decreased and are expected to decrease further in the medium term, while reserves held for the Enterprise M3 Local Enterprise Partnership (EM3 LEP) have increased as part of a deliberate strategy to ensure that major projects are approved based on the outcomes they will deliver rather than the speed at which funding provided by the Government can be spent.

5. Treasury Management and Prudential Indicators

5.1 The County Council's treasury management policy requires an annual report to the Cabinet on the exercise of the treasury management function, details of which are set out in Appendix 2. Under the Treasury Management Code of Practice, the end of year report has to be submitted to the County Council.

5.2 The Prudential Code for Capital Finance in Local Authorities requires that the County Council reports its actual performance against the Prudential Indicators that were set in its Treasury Management Strategy. Appendix 2 summarises the relevant indicators for the 2017/18 outturn which are in accordance with the figures approved by the County Council.

6. Capital Spending and Financing 2017/18

6.1 From the 2017/18 capital programme, schemes to the value of £221.5m were committed during the year, leaving £123.1m to be carried forward to 2018/19, subject to Cabinet's approval.

6.2 During 2017/18 capital expenditure of £208.7m was incurred, which can all be financed within available resources. This includes prudential borrowing of approaching £33.0 m. There will also be a further repayment of prudential borrowing from capital receipts and other funding sources of more than £12.5m. Further details of the outturn position for capital are provided in Appendix 3.

7. Assurance Statement

7.1 The code of Practice on Local Authority Accounting in the UK requires the County Council to publish, together with its Statement of Accounts, an annual governance statement signed by the Leader and Chief Executive. As part of this process, the Chief Internal Auditor provides an independent opinion on the adequacy and effectiveness of the system of internal control operating in the County Council as a whole. The Chief Internal Auditor's Annual Report and Opinion is approved by the Audit Committee.

7.2 The Chief Internal Auditor has concluded that:

"In my opinion, Hampshire County Council's framework of governance, risk management and management control is 'Adequate' and audit testing has demonstrated controls to be working in practice. Where weaknesses have been identified through internal audit review, we have worked with management to agree appropriate corrective actions and a timescale for improvement."

8. Pension Fund

8.1 The separate accounts for the Hampshire Pension Fund will also be incorporated in the County Council's Statement of Accounts. The accounts for 2017/18 record that the value of the fund's assets increased from £6.3bn to £6.6bn during the year. The Chief Internal Auditor has provided a separate assurance opinion for the Pension Fund and has concluded that:

"In my opinion, based on internal audit work completed 'Substantial Assurance' can be placed on Hampshire County Council (Pension Services) framework of governance, risk management and management control and audit testing has demonstrated controls to be working in practice. Where weaknesses have been identified through internal audit review, we have worked with management to agree appropriate corrective actions and a timescale for improvement."

9. Statutory Statement of Accounts

9.1 The Accounts and Audit Regulations 2015 introduced changes to the statutory accounting and audit timescales which have had a significant impact on the organisation. The changes came into effect for the preparation of the 2017/18 accounts.

9.2 This year the statement of accounts must be certified by the Chief Financial Officer (CFO) and submitted for external audit by 31 May, a month earlier than previously. Additionally, the audited accounts for 2017/18 must be published by 31 July, two months earlier than the previous timeframe.

9.3 Adopting an incremental approach, preparatory work has taken place over the last two financial years to achieve the new deadlines. For 2015/16, the deadline for CFO sign off of the accounts was brought forward by two weeks and for 2016/17 this was brought forward by a further two weeks to allow a trial run in anticipation of the changes coming into effect for the production of the 2017/18 accounts.

9.4 Achieving these challenging timescales has required concerted effort from across the organisation. The timetable was reviewed, following consultation with affected parties, and focused on what could be done either differently or earlier and what systems or processes could be changed to facilitate the achievement of the ultimate objective of a speedier accounting closure and production of the statement of accounts.

9.5 Meeting these earlier deadlines has been achieved through hard work across all departments in liaison with finance and our external auditors and the success this year in meeting the new timescales is noteworthy.

CORPORATE OR LEGAL INFORMATION:

Links to the Strategic Plan

Hampshire maintains strong and sustainable economic growth and prosperity:	Yes/~~No~~
People in Hampshire live safe, healthy and independent lives:	Yes/~~No~~
People in Hampshire enjoy a rich and diverse environment:	Yes/~~No~~
People in Hampshire enjoy being part of strong, inclusive communities:	Yes/~~No~~

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
Revenue Budget and Precept 2018/19 and Capital Programme 2018/19 – 2020/21 http://democracy.hants.gov.uk/ieDecisionDetails.aspx?AIId=6228	Cabinet – 5 February 2018 County Council – 22 February 2018
Medium Term Financial Strategy and Transformation to 2019 Savings Proposals http://democracy.hants.gov.uk/ieDecisionDetails.aspx?AIId=3194	Cabinet – 16 October 2017 County Council – 2 November 2017

IMPACT ASSESSMENTS:

1. Equality Duty

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.

Equalities Impact Assessment:

d) Equality objectives are not considered to be adversely impacted by the proposals in this report.

Impact on Crime and Disorder:

The proposals in this report are not considered to have any direct impact on the prevention of crime, but the County Council through the services that it provides through the revenue budget and capital programme ensures that prevention of crime and disorder is a key factor in shaping the delivery of a service / project.

Climate Change:

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

The revenue budget and capital programme contain measures that will assist in reducing our carbon footprint.

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

The County Council in designing its services will ensure that climate change issues are taken into account

Adults' Health and Care Department – Revenue Expenditure 2017/18

Major variations in cash limited expenditure – No variance against the adjusted cash limit.

Main Variations

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Director	(40)	(2.6)	
Strategic Commissioning and Business Support	(1,179)	(6.4)	Savings mainly relate to reduced spend on non care contracts, grants to voluntary organisations and staff budgets due to difficulty in recruiting to vacant posts.
Transformation	(159)	(3.8)	Savings mainly relate to additional income in relation to external courses provided by the workforce development team and staff budgets due to difficulty in recruiting to vacant posts.
Safeguarding, Quality and Governance	(110)	(3.0)	
Learning Disabilities and Mental Health	7,549	6.5	There are significant pressures on residential, homecare and direct payments due to an increase in client numbers and a delay in achieving savings. These pressures were partially offset by savings in supported living due in part to costs relating to previous financial years not materialising as anticipated. This position is not reflective of the longer term forecast for this service area as the full year effect of savings achieved in 2017/18 and new savings planned for 2018/19 are expected to bring the expenditure within budget from 2018/19.

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Older People and Physical Disabilities	(4,125)	(3.3)	There were pressures on both nursing and residential budgets due to higher client numbers and above budgeted weekly costs however, these pressures have been offset by savings in direct payments and homecare budgets where client numbers are less than budgeted. It should be noted that the budget includes non recurrent support of £5.6m from the Improved Better Care Fund (IBCF).
Internal Provision	411	0.9	The main area of pressure is within the Older Person's in-house homes due to the use of agency staff to cover vacant posts whilst permanent recruitment is undertaken. The County Council is required by the Care Quality Commission to have adequate staffing levels in order to retain its registration. This pressure has been offset by savings on other staffing budgets and reduced volumes of clients being referred to the REACT contract providers.
Contingencies	(2,347)	(99.1)	This mainly relates to the early achievement of Transformation to 2019 (Tt2019) savings and reduced spend on centrally held budgets.
Public Health	0	0.0	
Total	**0**	**0.0**	

Children's Services Department – Revenue Expenditure 2017/18

Major variations in cash limited expenditure – No variance against the adjusted cash limit.

Main variations

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Schools Budget			
Three to Four Year Olds Free Entitlement	(564)	(1.0)	The saving mainly relates to the actual take-up of the additional 15 hours (30 hours total) per week entitlement for eligible working families introduced from September 2017 being lower than estimated by the Department for Education (DfE), partly offset by a pressure on the standard 15 hours free entitlement for eligible 3 and 4 year olds due to the January census return leading to a large reduction in the Dedicated Schools Grant (DSG) funding.
Growth Fund	(558)	(11.2)	The position includes savings for infant class size funding, falling rolls, temporary classrooms, new / re-organising schools and growing schools, due to fewer schools being eligible for funding than budgeted.
Special Place Funding	1,282	6.4	This relates to a change in the way post 16 places were funded by the DfE in 2017/18 being reflected in the budgets.
Independent and Non-maintained Special Schools	4,203	28.0	The over spend is due to a 21% increase in the number of pupils placed in out of county provision (from 321 pupils in March 2017, to 389 pupils in March 2018), as well as an 18% increase in the average cost for SEN only pupils and 8% increase in the costs for joint funded pupils..

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
High Needs Top-Up Funding	4,940	11.4	The continuation in the growth of the number of high needs pupils in both maintained and special schools has exceeded budgetary expectations. This includes increasing numbers of pupils with Special Educational Needs Support Agreements (SENSA), an 8% annual increase in pupils with Education Health and Care Plans (EHCPs), an 11% increase in the numbers of high needs students in further education placements, additional placements in Other Local Authority schools and the continuation of the pressure on the service for discretionary payments from the previous financial year. These overs pends have been partly offset by a saving in Education Centre top-ups, following the implementation of the strategy to reintegrate more pupils back into mainstream education.
SEN Support Services	(784)	(14.1)	This largely relates to the £1m planned contingency, retained to offset arising pressures in the high needs block, partly offset by staffing cost pressures on the Specialist Teacher Advisory Service (STAS).
Central School Services	293	7.2	An over spend on the redundancy and premature retirement budget resulting from the budgetary pressures schools are facing leading to restructures and amalgamations that are increasing in-year redundancy, associated retirement and pay safeguarding costs.
Various other (net)	(455)	(0.1)	Various smaller budget savings across the Department.

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Carry Forward of Dedicated Schools Grant Deficit	(8,357)	(1.1)	The total 2017/18 over spend of £8.4m has been offset by a charge to the DSG reserve, as allowed by the DfE. This year, the charge will create a "deficit" on the DSG reserve of £4.5m, which it has been agreed by Schools Forum will be funded from future years DSG funding.
Sub-Total Schools Budget	**0**	**0.0**	
Non-Schools Budget			
Home to School Transport	(507)	(2.0)	Although costs within the Home to School Transport budget are rising as a result of increased demand for school age and post-16 SEN transport, various one-off accounting adjustments relating to historic balances have led to a technical saving this financial year.
Children Looked After (CLA placements)	(32)	0.0	Unprecedented activity and cost increases across CLA placements, care leavers and Unaccompanied Asylum Seekers (UASC) have seen an annual increase in expenditure of 14% on the previous year. This has been closely monitored throughout the year, and as a result additional corporate funding of £9.5m on an ongoing basis, plus a further £7.2m on a one-off basis has been provided to offset what would otherwise have been a very significant pressure. The underlying pressure has mainly arisen on Non-County Placements (NCPs), which required over half of the additional corporate funding due to a 17% increase in costs, mainly as a result of increased activity

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Special Guardianship (SGO) support	584	26.0	The over spend is due to a 16% increase in the number of SGOs, from 381 in March 2017 to 442 in March 2018. On 1 February 2018 the SGO rate was increased to match the current in-house fostering rate. This has a full year cost of £1.2m (£203,000 part year cost this financial year), which will be met from additional corporate funding.
Respite for disabled children	(620)	(10.0)	Including a saving on short break activities with commitments for care support in the community not being fully utilised and the continuation from the previous financial year of lower than budgeted spend on overnight respite.
Youth Justice	764	37.5	Lower income at Swanwick Lodge Secure Unit as a result of severe staff shortages and problems with the heating system in the unit reducing the numbers of available beds below target occupancy levels. This has been offset by a partial return of HCC's contribution to the Hampshire Youth Offending Team (YOT) due to the sustainability of the Partnership's budget, and a reduction in number of placements relating to direct remands.
Safeguarding & Young People's Services	2,269	12.0	The pressure mainly results from the use of social work agency staff to cover for the short supply of qualified social workers. Corporate support has been agreed to increase the numbers of social workers, leading to a reduced caseload for teams and thereby increasing retention of social workers and reducing the need for agency staff. This investment commenced in 2017/18.
Early Achievement of T2019 Savings	(755)	(100.0)	Planned early achievement of savings in relation to the Tt2019 Programme, used to offset the Department's other pressures.

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Various other (net)	(1,580)	(1.0)	Various smaller budget savings across the Department.
Contribution from Cost of Change	(123)		
Sub-Total Non-Schools Budget	**0**	**0.0**	
Total	**0**	**0.0**	

Economy, Transport & Environment Department – Revenue Expenditure 2017/18

Major variations in cash limited expenditure – Savings of £5.0m (4.5%) against the adjusted cash limit.

Main Variations

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Highways, Traffic & Transport	(3,813)	(6.3)	The position reflects savings against the winter maintenance budget of £644,000, which Cabinet has agreed in principle to reinvest in highways maintenance in 2018/19, providing additional one-off resources to supplement existing planned maintenance programmes. In addition, the annual Bus Service Operator Grant (BSOG) has previously been used to support additional investment in improving bus passenger amenities, such as offering grants attracting match funding for investment in contactless payment. From 2019/20 the annual BSOG is built in to ETE savings proposals to support subsidised bus services. Therefore the 2017/18 BSOG grant of circa £1.3m was added to the bus subsidy budget to enable a planned early saving of a broadly equivalent amount from the bus subsidy budget for 2017/18. It is planned to utilise the funding resulting from this saving to increase ETE's Cost of Change to help cash flow the Department's Tt2019 overall savings proposals. It is expected that additional cash flow funding will be required, especially in relation to realisation of planned savings within the waste management budget, following recent Government policy announcements about recycling and the proposed deposit return scheme for drinks containers. It is then planned to use BSOG directly to manage the implementation of the reduced bus subsidy budget from 2019/20.

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
			The outturn also reflects: • A small saving on highways maintenance with offset by additional fee income relating to the HCC capital programme (£860,000 net saving) • £227,000 one-off net benefit in Strategic Transport from a technical adjustment relating to previous year fee income from road agreements. • £521,000 savings against the Concessionary Fares budget due to fewer journeys being made • The cumulative effect of various other smaller savings, including as a result of active vacancy management.
Economic Development and Research & Intelligence	(118)	(10.1)	The outturn figures reflect in-year savings as a result of staff vacancies and the impact of delays in planned expenditure, which will now take place in 2018/19.
Waste, Planning & Environment	(496)	(1.1)	The savings predominantly relate to vacancy management and additional income including trading for example from the Minerals and Waste Planning work for Berkshire authorities (Strategic Planning and Environment). In addition, there were minor savings against the Waste budget.

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Early Delivery of Tt2019 savings and General Departmental	(555)	(25.5)	The identification of opportunities for the early delivery of Tt2019 savings has resulted in savings of £1.25m being achieved in 2017/18. Any early delivery of savings enables the Department to fund costs associated with transformation and the delivery of remaining savings targets. This in-year saving was partly used to fund expenditure of £954,000 on projects delivered during 2017/18, with the balance added to the Department's Cost of Change reserve. In addition, various ongoing active housekeeping savings of £259,000 were achieved across departmental non-pay budgets.
Total	**(4,982)**	**(4.5)**	

Policy and Resources Department – Revenue Expenditure 2017/18

Major variations in cash limited expenditure – Savings of £5.5m (5.0%) against the adjusted cash limit.

Main Variations

Service Area	**Variance (Under) / Over Budget** £'000	%	**Reason for Variation**
Culture, Community and Business Services	(595)	(1.9)	Progress has been made in achieving the Department's Tt2019 savings target, resulting in the early delivery of savings of more than £1.5m in 2017/18. In addition, a further planned saving of more than £2.3m has been achieved. This is predominantly the result of cost savings and re-phased planned project expenditure which will now be undertaken during 2018/19 (mainly the Library Service and Office Accommodation), vacancy management savings (Trading Standards, Business Support and Asbestos) and additional income generation (Registration, Property Direct Services and Great Hall). The early achievement of Tt2019 savings, other in-year savings and a draw of £131,000 from the accumulated Cost of Change reserve has allowed one-off investment of approaching £4m to be made to fund transformational projects across the Department to support the achievement of Tt2019 savings targets. In addition, the agreed transfer of the in-year PrintSmart contract outturn of £0.7m has been made to a separate reserve.

Service Area	Variance (Under) / Over Budget £'000	%	Reason for Variation
Corporate Services	(4,052)	(7.0)	Corporate Services continues to implement a strategy of strong budgetary control, managing expenditure through joint working and generating income, for example for legal and other services. This has enabled the costs to support the Tt2019 Programme to be absorbed and also ensured early achievement of Tt2019 savings to contribute to the cost of change reserve to be used for future investment in further transformation work.
Non Departmental Policy & Resources	(804)	(3.9)	The saving largely reflects lower costs or additional income in a number of budget areas. This includes lower members support costs mostly due to pensions change for members after election and lower Rural Affairs expenditure during 2017/18 which will be carried forward to match future expenditure.
Total	**(5,451)**	**(5.0)**	

Treasury Management Outturn Report 2017/18

1. Summary

1.1. The County Council adopted the key recommendations of the Chartered Institute of Public Finance and Accountancy's (CIPFA) Treasury Management in the Public Services: Code of Practice in February 2010. These recommendations include approving an annual report on treasury management activity after the end of each financial year.

1.2. This report fulfils the County Council's legal obligation to have regard to the CIPFA Code.

1.3. The County Council's Treasury Management Strategy (TMS) for 2017/18 was approved at a meeting of full Council in February 2017. 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 risk are therefore central to the County Council's TMS.

1.4. Treasury management in the context of this report is defined as:

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

1.5. This annual report sets out the performance of the treasury management function during 2017/18, to include the effects of the decisions taken and the transactions executed in the past year.

1.6. Overall responsibility for treasury management remains with the County Council. No treasury management activity is without risk; the effective identification and management of risk are integral to the County Council's treasury management objectives.

1.7. All treasury activity has complied with the County Council's TMS and Investment Strategy for 2017/18, and all relevant statute, guidance and accounting standards. In addition the County Council's treasury advisers, Arlingclose, provide support in undertaking treasury management activities. The County Council has also complied with all of the prudential indicators set in its TMS.

2. External Context

2.1. The following sections outline the key economic themes currently in the UK against which investment and borrowing decisions were made in 2017/18.

Economic commentary

2.2. The UK economy showed signs of slowing with latest estimates showing GDP, helped by an improving global economy, grew by 1.8% in 2017, the same level as in 2016. This was a far better outcome than the majority of forecasts following the EU Referendum in June 2016, but it also reflected the international growth momentum generated by the increasingly buoyant US economy and the re-emergence of the Eurozone economies.

2.3. The inflationary impact of rising import prices, a consequence of the fall in Sterling associated with the EU referendum result, resulted in year-on-year CPI rising to 3.1% in November before falling back to 2.7% in February 2018. Consumers felt the squeeze as real average earnings growth, i.e. after inflation, turned negative before slowly recovering. The labour market showed resilience as the unemployment rate fell back to 4.3% in January 2018. The inherent weakness in UK business investment was not helped by political uncertainty following the surprise General Election in June 2017 and by the lack of clarity on Brexit. The Withdrawal Treaty is yet to be ratified by the UK Parliament and those of the other 27 EU member states and new international trading arrangements are yet to be negotiated and agreed.

2.4. The Bank of England's Monetary Policy Committee (MPC) increased the Bank Rate by 0.25% in November 2017. This action was significant as this was the first rate increase in ten years, although in essence the MPC reversed its August 2016 cut following the referendum result. The February Inflation Report indicated the MPC was keen to return inflation to the 2% target over a more conventional (18 - 24 month) horizon with 'gradual' and 'limited' policy tightening. Although in March two MPC members voted to increase policy rates immediately and the MPC itself stopped short of committing itself to the timing of the next increase in rates, the minutes of the meeting suggested that an increase in May 2018 was highly likely, however at the meeting in May 2018 the MPC again voted by a majority of 7-2 to maintain Bank Rate at 0.5%.

Credit background

2.5. The rules for UK banks' ring-fencing were finalised by the Prudential Regulation Authority and banks began the complex implementation process ahead of the statutory deadline of 1 January 2019. As there was some uncertainty surrounding which banking entities the County Council would be dealing with once ring-fencing was implemented and what the balance sheets of the ring-fenced and non ring-fenced entities would look like, in May 2017 Arlingclose advised adjusting downwards the maturity limit for unsecured investments to a maximum of six months. The rating agencies had slightly varying views on the creditworthiness of the restructured entities.

2.6. Barclays was the first to complete its ring-fence restructure over the 2018 Easter weekend; wholesale deposits including local authority deposits will henceforth be accepted by Barclays Bank plc (branded Barclays International), which is the non ring-fenced bank.

2.7. In March 2018, following Arlingclose's advice, the County Council removed RBS plc and National Westminster Bank from its counterparty list for unsecured investments. This did not reflect any change to the creditworthiness of either bank, but a tightening in Arlingclose's recommended minimum credit rating criteria to A- from BBB+ for 2018/19. The current long-term ratings of RBS and NatWest do not meet this minimum criterion, although if following ring-fencing NatWest is upgraded, the bank would be reinstated on the County Council's unsecured lending list.

Local Authority Regulatory Changes

2.8. CIPFA published revised editions of the Treasury Management and Prudential Codes in December 2017. The 2017 Prudential Code introduces the requirement for a Capital Strategy which provides a high-level overview of the long-term context of capital expenditure and investment decisions and their associated risks and rewards along with an overview of how risk is managed for future financial sustainability. Where this strategy is produced and approved by full Council, the determination of the Treasury Management Strategy (TMS) can be delegated to a committee. The Code also expands on the process and governance issues of capital expenditure and investment decisions. The County Council will be preparing the Capital Strategy in line with the 2019/20 budget setting process.

2.9. In the 2017 Treasury Management Code the definition of 'investments' has been widened to include financial assets as well as non-financial assets held primarily for financial returns such as investment property. These, along with other investments made for non-treasury management purposes such as loans supporting service outcomes and investments in subsidiaries, must be discussed in the Capital Strategy or Investment Strategy. Additional risks of such investments are to be set out clearly and the impact on financial sustainability is be identified and reported.

MiFID II

2.10. As a result of the second Markets in Financial Instruments Directive (MiFID II), from 3 January 2018 local authorities were automatically treated as retail clients but could "opt up" to professional client status, providing certain criteria were met which include having an investment balance of at least £10m and the person(s) authorised to make investment decisions on behalf of the authority having at least one year's relevant professional experience. In addition, the regulated financial services firms to whom this directive applies have had to assess that the person(s) have the expertise, experience and knowledge to make investment decisions and understand the risks involved.

2.11. The County Council has met the conditions to opt up to professional status and has done so in order to maintain its previous MiFID status prior to January 2018. The County Council will continue to have access to products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice.

3. Local Context

3.1. At 31 March 2018 the County Council's underlying need to borrow for capital purposes as measured by the Capital Financing Requirement (CFR) was £764m, while usable reserves and working capital which are the underlying resources available for investment were £571m (principal invested plus gains on investments with a variable net asset value). These factors and the year-on-year change are summarised in Table 1 below:

Table 1: Balance Sheet Summary

	Balance 31/03/2017 £m	Movement £m	Balance 31/03/2018 £m
CFR	(755.4)	(8.6)	(764.0)
Less: Other debt liabilities*	171.0	(6.8)	164.2
Borrowing CFR	(584.4)	(15.4)	(599.8)
Less: Resources for investment	522.2	48.5	570.7
Net borrowing	(62.2)	33.1	(29.1)

* finance leases and PFI liabilities that form part of the County Council's debt.

3.2. Although CFR has risen as new capital expenditure was higher in comparison to the amount of debt paid in 2017/18, net borrowing has decreased overall due to an increase in usable reserves. The increase in usable reserves is partly due to capital grants unapplied received in advance of spend, as well as an increase in the Grant Equalisation Reserve (GER) to enable the County Council to continue its financial strategy, and to allow delivery of the more complex savings to be achieved within the Transformation to 2019 (Tt2019) Programme over the two years.

3.3. The County Council's strategy was to maintain borrowing and investments below their underlying levels, referred to as internal borrowing, in order to reduce risk and keep interest costs low. The treasury management position as at 31 March 2018 and the year-on-year change is shown in Table 2 below:

Table 2: Treasury Management Summary

	31/03/17 Balance £m	Movement £m	31/03/18 Balance £m	31/03/18 Rate %
Long-term borrowing	(319.7)	39.7	(280.0)	(4.59)
Short-term borrowing	(13.6)	5.7	(7.9)	(3.28)
Total Borrowing	**(333.3)**	**45.5**	**(287.8)**	**(4.55)**
Long-term investments	277.5	11.8	289.3	2.72
Short-term investments	160.1	80.4	240.5	1.30
Cash and cash equivalents	75.5	(43.1)	32.4	0.45
Total Investments	**513.1**	**49.1**	**562.2**	**1.98**
Net Investments	**179.8**	**94.6**	**274.4**	

Note: The figures in the table above are from the balance sheet in the County Council's statement of accounts, adjusted to exclude operational cash, accrued interest and other accounting adjustments.

3.4. The County Council's internal borrowing policy is the reason for the large variance between the positions shown in Tables 1 and 2. The movement that has taken place during 2017/18 in net borrowing shown in Table 1 has translated into a rise in investment balances as shown in Table 2. In addition, total borrowing in Table 2 has reduced during 2017/18 due to the early repayment of £32m of long-term borrowing in the form of LOBO (Lender's Option, Borrower's Option) loans and repayment upon maturity of £13.6m of Public Works Loan Board (PWLB) debt.

4. Borrowing Activity

4.1. At 31 March 2018 the County Council held £288m of loans, a decrease of £45m on the previous year, as part of its strategy for funding previous years' capital programmes. The year-end treasury management borrowing position and year-on-year change is shown in Table 3 below; which excludes borrowing taken out on behalf of others:

Table 3: Borrowing Position

	31/03/17 Balance £m	Movement £m	31/03/18 Balance £m	31/03/18 Rate %	31/03/18 WAM* Years
Public Works Loan Board	257.0	(13.6)	243.4	4.66	11.03
Banks (LOBO)	60.0	(40.0)	20.0	4.76	15.29
Banks (fixed term)	13.0	8.0	21.0	4.21	21.91
Total Borrowing	**330.0**	**45.6**	**284.4**	**4.63**	**12.13**

* Weighted average maturity

Note: the figures in the table above are from the balance sheet in the County Council's statement of accounts, but adjusted to exclude borrowing taken out on behalf of others, and accrued interest.

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

4.3. Affordability and the "cost of carry" remained important influences on the County Council's borrowing strategy alongside the consideration that, for any borrowing undertaken ahead of need, the proceeds would have to be invested in the money markets at rates of interest significantly lower than the cost of borrowing. As short-term interest rates have remained and are likely to remain at least over the forthcoming two years, lower than long-term rates, the County Council determined it was more cost effective in the short-term to use internal resources instead of taking out new borrowing. This strategy enabled the County Council to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk.

4.4. The benefits of internal borrowing were monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Arlingclose assists the County Council with the monitoring of internal and external borrowing.

4.5. During 2017/18 the County Council repaid £13.6m of maturing PWLB debt, and did not replace this borrowing. This will reduce the future cost of interest payments on the County Council's external debt.

4.6. The County Council continues to hold £41m of market loans (£20m of which are LOBO loans, and £21m of which were LOBO but have now been converted to fixed term loans by the lender); this has reduced from the £73m historical balance due to the County Council having negotiated the early repayment of £32m of LOBO loans, and repaid these at a saving in comparison to the total cost expected over the loans' lifetime. LOBO loans are 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. None of the LOBO loan options were exercised by the lender in the year.

5. Investment Activity

5.1. The County Council holds invested funds representing income received in advance of expenditure plus balances and reserves held. During 2017/18 the Council's investment balances have ranged between £513m and £659m due to timing differences between income and expenditure. The year-end investment position and the year-on-year change are shown in Table 4 overleaf:

Table 4: Investment Position (Treasury Investments)

Investments	31/03/17 Balance £m	Movement £m	31/03/18 Balance £m	31/03/18 Rate %	31/03/18 WAM* years
Short term Investments					
- Banks and Building Societies:					
- Unsecured	35.7	(24.0)	11.7	0.53	0.11
- Secured	20.0	35.0	55.0	1.00	0.56
- Money Market Funds	61.7	(36.0)	25.7	0.46	0.00
- Local Authorities	116.8	43.7	160.5	1.33	0.35
- Corporate Bonds	1.3	(1.3)			
- Registered Provider		20.0	20.0	2.03	0.33
	235.6	**37.3**	**272.9**	**1.20**	**0.35**
Long term Investments					
- Banks and Building Societies:					
- Secured	70.0	8.3	78.3	0.79	2.57
- Local Authorities	97.5	(36.5)	61.0	1.41	1.94
	167.5	**(28.2)**	**139.3**	**1.06**	**2.29**
Long term Investments – high yielding strategy					
- Local Authorities					
- Fixed deposits	20.0		20.0	3.96	15.97
- Fixed bonds	10.0		10.0	3.78	15.77
- Pooled Funds					
- Pooled property**	45.0	10.0	55.0	4.60	N/A
- Pooled equity**	20.0	20.0	40.0	4.28	N/A
- Pooled multi-asset**	10.0	10.0	20.0	3.99	N/A
- Registered Provider	5.0		5.0	3.40	1.08
	110.0	**40.0**	**150.0**	**4.25**	**13.79**
Total Investments	**513.1**	**49.1**	**562.2**	**1.98**	**2.00**

* Weighted average maturity

** The rates provided for pooled fund investments are reflective of the average of the most recent dividend return as at 31 March 2018.

Note: the figures in the table above are from the balance sheet in the County Council's statement of accounts, but adjusted to exclude operational cash, accrued interest and other accounting adjustments.

5.2. Both the CIPFA Code and the government guidance require 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.

5.3. In furtherance of these objectives, and given the increasing risk and low returns from short-term unsecured bank investments, the County Council further diversified into more secure and higher yielding asset classes during 2017/18. For example, the proportion of investments to liquid funds (i.e. invested in money market funds and unsecured call accounts) was reduced and instead invested in secure short-term investments with higher rates of return (such as local authorities). Also £40m was added to externally-managed funds during 2017/18 as part of the investments targeting higher yields.

5.4. Security of capital has remained the County Council's main investment objective. This has been maintained by following the County Council's counterparty policy as set out in its Treasury Management Strategy Statement for 2017/18.

5.5. Counterparty credit quality was assessed and monitored with reference to credit ratings, for financial institutions analysis of funding structure and susceptibility to bail-in, credit default swap prices, financial statements, information on potential government support and reports in the quality financial press.

5.6. The County Council will also consider the use of secured investments products that provide collateral in the event that the counterparty cannot meet its obligations for repayment.

5.7. The County Council maintained a sufficient level of liquidity through the use of call accounts and money market funds. The County Council sought to optimise returns commensurate with its objectives of security and liquidity. The UK Bank Rate increased by 0.25% to 0.50% in November 2017 and short-term money market rates have remained at relatively low levels which continued to have a significant impact on cash investment income.

5.8. The progression of credit risk and return metrics for the County Council's investments managed in-house (excluding external pooled funds) are shown in the extracts from Arlingclose's investment benchmarking in Table 5 below:

Table 5: Investment Benchmarking (investments managed in-house)

	Credit Rating	Bail-in Exposure	WAM* (days)	Rate of Return
31/03/2017	AA	22%	709	1.21%
31/03/2018	AA	8%	735	1.36%
Similar Local Authorities	AA-	48%	879	0.94%
All Local Authorities	AA-	55%	35	0.63%

* Weighted average maturity

5.9. As part of the 2017/18 Investment Strategy the total amount targeted towards high yielding investments was increased to £200m. Investments yielding higher returns will contribute additional income to the County Council, although some come with the risk that they may suffer falls in the value of the principal invested.

5.10. Of the £200m available £150m has been invested (an increase of £40m since 31 March 2017), and an additional £10m has been committed but not called.

5.11. The £115m portfolio of externally managed pooled multi-asset, equity and property funds generated an average total return of 4.9%, comprising 4.88% income return used to support services in year, and 0.02% of capital growth. As 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 are regularly reviewed.

5.12. The investments in pooled funds allow the County Council to diversify into asset classes other than cash without the need to own and manage the underlying investments. The funds which are operated on a variable net asset value (VNAV) basis offer diversification of investment risk, coupled with the services of a professional fund manager; they also offer enhanced returns over the longer term but are more volatile in the short-term. All of the County Council's pooled fund investments are in the respective fund's distributing share class which pay out the income generated.

5.13. Although money can 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.

5.14. The 2015/16 Investment Strategy recommended that the returns from a pooled property fund be used to contribute £0.5m each year to a reserve in the County Council's accounts as protection against the irrecoverable fall in value of any investments. It is now recommended that £0.5m is added to this reserve in line with this strategy to further protect the County Council's funds. This is prudent given the additional risk that is being taken in targeting investments with higher returns and will bring the total amount in the reserve to £2m.

6. Other Non-Treasury Holdings and Activity

6.1. Although not classed as treasury management activities the Council may also make loans and investments for service purposes, for example loans to Hampshire based businesses or the direct purchase of land or property. Such loans and investments will be subject to the Council's normal approval processes for revenue and capital expenditure and need not comply with this treasury management strategy. The County Council's existing non-treasury investments are listed in Table 6 overleaf:

Table 6: Non-Treasury Investments

	31/03/18 Asset Value £m	31/03/18 Rate %
Loans to Hampshire based business	5.75	4.00
Total	**5.75**	**4.00**

7. Compliance Report

7.1. The County Council confirms compliance of all treasury management activities undertaken during 2017/18 with the CIPFA Code of Practice and the County Council's approved TMS. Compliance with specific investment limits, as well as the authorised limit and operational boundary for external debt, is demonstrated in Tables 7 and 8 below:

Table 7: Debt Limits

	2017/18 Maximum £m	31/03/18 Actual £m	2017/18 Operational Boundary £m	2017/18 Authorised Limit £m	Complied
Borrowing	333	284	680	740	✓
Other long term liabilities	171	164	170	210	✓
Total Debt	**504**	**448**	**850**	**950**	✓

Table 8: Investment Limits

	2017/18 Maximum £m	31/03/18 Actual £m	2017/18 Limit £m	Complied
Any single organisation, except the UK Central Government	40	23	70	✓
Any group of organisations under the same ownership	40	23	70	✓
Any group of pooled funds under the same management	30	30	70	✓
Registered providers	25	25	70m	✓
Money market funds	19%	5%	50%	✓

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. This indicator is set to control the County Council's exposure to interest rate risk. The upper limits on fixed and variable rate interest rate exposures, expressed as the amount of net principal borrowed will be:

Table 9 – Interest Rate Exposures

	31/03/18 Actual £m	2017/18 Limit £m	Complied
Upper limit on fixed interest rate investment exposure	90	375	✓
Upper limit on variable interest rate investment exposure	473	700	✓
Upper limit on fixed interest rate borrowing exposure	277	960	✓
Upper limit on variable interest rate borrowing exposure	8	960	✓

✓

8.3. Fixed rate investments and borrowings are those where the rate of interest is fixed for the whole financial year. Instruments that mature during the financial year are classed as variable rate.

Maturity Structure of Borrowing

8.4. 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 10 – Maturity Structure of Borrowing

	31/03/18 Actual	Upper Limit	Lower Limit	Complied
Under 12 months	3%	50%	0%	✓
12 months and within 24 months	3%	50%	0%	✓
24 months and within 5 years	10%	50%	0%	✓
5 years and within 10 years	17%	75%	0%	✓
10 years and within 20 years	56%	75%	0%	✓
20 years and within 30 years	11%	75%	0%	✓
30 years and above	0%	100%	0%	✓

Principal Sums Invested for Periods Longer than 364 days

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 total principal sum invested to final maturities beyond the period end will be:

Table 11 – Principal Sums Invested for Periods Longer than 364 days

	2017/18 £m	2018/19 £m	2019/20 £m
Actual principal invested beyond year end	280	227	173
Limit on principal invested beyond year end	375	300	300
Complied	✓	✓	✓

Capital Spending and Financing 2017/18

1 Introduction

1.1 This Appendix reports that:

- Capital schemes costing £221.5m were started during 2017/18 from the approved capital programme for the year of £355.9m.
- This left £123.1m for named projects not started by 31 March 2018 which will be carried forward to 2018/19, subject to Cabinet's approval.
- Capital payments of £208.7m were incurred in 2017/18 and this can be financed within available resources.
- It is proposed that, under the Prudential Code for Capital Finance, new prudential borrowing of £33.0m is used in 2017/18 to fund previously approved schemes. Government grant support will not be available to finance this borrowing.
- Repayments of prudential borrowing from capital receipts and other sources total £12.5m in 2017/18.
- £14.1m of surplus resources will be added to the capital reserve in 2017/18 for use in funding future payments.
- Capital receipts of £27.3m were achieved from the sale of assets in 2017/18.

2 Capital Programme for 2017/18

2.1 Table 1 below shows that 62.2% of the capital programme for 2017/18 of £221.5m was started in the year.

Table 1 - Capital Schemes Committed in 2017/18

	£'000	%
Approved value of the capital programme for 2017/18	355,874	100.0
Schemes committed in 2017/18	221,447	62.2
Balance of Cash Limit at 31 March 2018	**134,427**	**37.8**
Schemes for which approval to carry forward to 2018/19 is now requested	123,058	34.6
Schemes previously approved for carry forward	11,369	3.2
Total Cash Limit to be Carried Forward to 2018/19	**134,427**	**37.8**

2.2 An analysis by service of the figures in Table 1 is included in Annex 1.

3. Carry Forward of Schemes not Committed by 31 March 2018

3.1 The approval of Cabinet is required for proposals to carry forward schemes not started at 31 March 2018. The total value of such schemes is £123.1m. This excludes £11.4m of Children's Services schemes for which approval to carry forward to 2018/19 has previously been given during 2017/18. These amounts are largely committed against named projects.

3.2 As Table 2 shows, the value of the 2017/18 programme committed in the year, at £221.5m, is higher than the level achieved in 2016/17 of £196.5. Good progress is being made given the significant size of the overall capital programme.

Table 2 – Percentage of Capital Programme Committed

	2016/17 £m	2017/18 £m
Value of Projects		
- Committed	196.5	221.5
- Carried forward	121.6	134.4
Total Programme	**318.1**	**355.9**
Percentage Committed	61.2%	62.2%

3.3 Individually, most of the schemes and provisions to be carried forward are relatively small amounts. The larger schemes include:

- Adults with Disability – Accommodation Strategy (£9.4m) – A capital grants programme has been approved and is progressing.
- Extra care housing transformation (£20.2m) – Projects are being considered.
- Children's Services contingency provision carried forward to cover future projects and pressures on the capital programme (£26.0m).
- Structural maintenance of roads and bridges – Future projects planned which are linked to the outcome of funding bids (£20.8m).
- Infrastructure and utility works (£15.7m) – Project designs are progressing.
- Investment in Hampshire projects – Projects are planned (£3.0m).

4. Capital Expenditure and Financing 2017/18

4.1 Total expenditure actually incurred in 2017/18, arising from the capital programme for 2017/18 and earlier years, was £208.7m. This is £29.4m or 12.4% lower than the revised estimate for 2017/18. The timing of capital expenditure flows between financial years is often difficult to predict. The delays in committing a fair proportion of the capital programme for 2017/18, as shown in Table 2, will have reduced the level of payments in the year.

4.2 An analysis of the expenditure of £208.7m by service and type is included in Annex 2.

4.3 The proposed method of financing this expenditure is summarised in Table 3:

Table 3 – Capital Financing 2017/18

	Adjusted Revised Estimate £'000	**Actuals £'000**	**Variation £'000**
Prudential borrowing			
- for capital schemes	37,097	32,959	(4,138)
- repayments of specific schemes	(10,199)	(12,553)	(2,354)
Government capital grants	92,020	93,566	1,546
Contributions from developers and outside agencies	59,205	66,810	7,605
Capital receipts	5,880	27,327	21,447
Revenue reserves	1,167	1,761	594
Revenue contributions			
- general corporate provision	12,947	12,947	0
Total Capital Resources	**198,117**	**222,817**	**24,700**
Transfers from / (to) capital reserve	41,009	0	(41,009)
- planned use of capital reserve to fund payments	(1,052)	(14,153)	(13,101)
Total funding for payments in 2017/18	**238,074**	**208,664**	**(29,410)**

4.4 In addition to this spend, during 2017/18, the Enterprise M3 Local Enterprise Partnership (LEP) invested £16.9m in Capital projects within the M3 corridor. This spend is included in the annual accounts, as the Council is the Accountable Body for the LEP.

5. Borrowing

5.1 Since 1 April 2004, local authorities have been permitted to borrow for capital purposes without specific approval from the Government, provided their actions meet the requirements of the Prudential Code for Capital Finance introduced by the Local Government Act 2003. This is known as 'prudential borrowing'. It does not attract any support from the Government towards the repayment and interest costs, which fall wholly on the County Council's own resources.

5.2 Cabinet agreed criteria for the use of prudential borrowing in November 2003, with revisions in February 2006. Since then, its use has been agreed for a number of capital schemes, primarily on an invest-to-save basis. It is proposed that a total of £33m is borrowed in 2017/18 for these schemes, in accordance with the approved criteria.

5.3 Prudential borrowing of £12.5m has been repaid in 2017/18 from the use of capital receipts, developer and other contributions.

5.4 The Prudential Code includes a number of indicators intended to illustrate whether local authorities are acting prudently. The County Council's latest position on these prudential indicators following the 2017/18 outturn is summarised in Appendix 2. It shows that the County Council continues to be in full compliance with the requirements of the Code.

6. Capital receipts

6.1 Capital receipts from the sale of land and property in 2017/18 were £27.3m in total. This has been used to fund capital expenditure in the year.

6.2 Services' proposed shares of capital receipts in 2017/18 are summarised in Annex 3. The County Council's policy allows services to retain 25% of capital receipts from the sale of their assets, with up to 100% for approved rationalisation schemes.

6.3 In line with this policy, services are entitled to £12.6m of the £27.3m received in 2017/18. Cabinet has previously approved the addition of the majority of this amount to services' capital programmes, leaving a total of £0.3m for which approval is now required for allocation to services, as set out in Annex 3.

Analysis of Capital programme 2017/18 and Requests by Services to Carry Forward Capital Schemes to 2018/19

	(1) Approved Value of Programme	(2) Schemes Committed in 2017/18	(3) Schemes for Which Approval to Carry Forward is Requested	(4) Schemes Already Approved for Carry Forward	Total Cash Limit Carried Forward to 2018/19 (Columns 3+4)
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Adults' Services	55,127	24,008	31,119		31,119
Children's Services	146,777	101,198	34,210	11,369	45,579
Economy, Transport and Environment	81,248	52,201	29,047		29,047
Policy and Resources	72,722	44,040	28,682		28,682
Total	**355,874**	**221,447**	**123,058**	**11,369**	**134,427**
	100.0%	62.2%	34.6%	3.2%	37.8%

The amounts to be carried forward are largely committed against named projects

Summary of Capital Expenditure in 2017/18

Analysis by service

	£'000	%
Adults' Services	25,090	12.0
Children's Services	62,261	29.9
Economy, Transport and Environment	74,542	35.7
Policy and Resources	46,771	22.4
	208,664	**100.0**

Analysis by type of expenditure

	£'000	%
Land	3,645	1.7
Construction work	143,089	68.6
Fees and salaries	25,622	12.3
Furniture, equipment and vehicles	17,741	8.5
Grants	14,132	6.8
Capital Loan	4,435	2.1
	208,664	**100.0**

Analysis of Capital Receipts 2017/18

	Net Capital Receipts	Costs of Sales	Shares from in/out and Other Schemes		25% Share of Qualifying Receipts Now Due to Services
			Previously Added to Programme	Now Available to be Added to Programme	
	£'000	**£'000**	**£'000**	**£'000**	**£'000**
Adults' Services					
Children's Services	7,445		7,445		
Economy, Transport and Environment	113	1	113		
Policy and Resources	19,769		4,999	290	
	27,327	**1**	**12,557**	**290**	**0**

Total Now to be Added to Services' Programmes	**290**