

# Governance, Audit, Risk Management and Standards Committee Agenda

**Date:** Tuesday 25 January 2022

**Time:** 6.30 pm

**Venue:** Virtual Meeting - Online

## Membership (Quorum 3)

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|                                      |  |
|--------------------------------------|--|
| <b>Chair:</b>                        | Councillor David Perry   |
| <b>Labour Councillors:</b>           | Dean Gilligan<br>Kairul Kareema Marikar<br>Antonio Weiss       |
| <b>Conservative Councillors:</b>     | Philip Benjamin<br>Amir Moshenson<br>Kanti Rabadia (VC)        |
| <b>Labour Reserve Members:</b>       | 1. Niraj Dattani<br>2. Chloe Smith<br>3. Vacancy<br>4. Vacancy |
| <b>Conservative Reserve Members:</b> | 1. Pritesh Patel<br>2. John Hinkley<br>3. Hitesh Karia         |

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# Useful Information

## Meeting details:

This meeting is open to the press and public and can be viewed on [www.harrow.gov.uk/virtualmeeting](http://www.harrow.gov.uk/virtualmeeting)

**Agenda publication date: Monday 17 January 2022**

# Agenda - Part I

## 1. Attendance by Reserve Members

To note the attendance at this meeting of any duly appointed Reserve Members.

Reserve Members may attend meetings:-

- (i) to take the place of an ordinary Member for whom they are a reserve;
- (ii) where the ordinary Member will be absent for the **whole** of the meeting; and
- (iii) the meeting notes at the start of the meeting at the item 'Reserves' that the Reserve Member is or will be attending as a reserve;
- (iv) if a Reserve Member whose intention to attend has been noted arrives after the commencement of the meeting, then that Reserve Member can only act as a Member from the start of the next item of business on the agenda after his/her arrival.

## 2. Declarations of Interest

To receive declarations of disclosable pecuniary or non pecuniary interests, arising from business to be transacted at this meeting, from:

- (a) all Members of the Committee;
- (b) all other Members present.

## 3. Minutes (Pages 5 - 12)

That the minutes of the meeting held on 30 November 2021 be taken as read and signed as a correct record.

## 4. Public Questions \*

To receive any public questions received in accordance with Committee Procedure Rule 17 (Part 4B of the Constitution).

Questions will be asked in the order in which they were received. There will be a time limit of 15 minutes for the asking and answering of public questions.

**[The deadline for receipt of public questions is 3.00 pm, 20 January 2022.**

**Questions should be sent to [publicquestions@harrow.gov.uk](mailto:publicquestions@harrow.gov.uk)**

**No person may submit more than one question].**

## 5. Petitions

To receive petitions (if any) submitted by members of the public/Councillors under the provisions of Committee Procedure Rule 15 (Part 4B of the Constitution).

## 6. Deputations

To receive deputations (if any) under the provisions of Committee Procedure Rule 16 (Part 4B) of the Constitution.

## 7. References from Council and other Committees/Panels

To receive references from Council and any other Committees or Panels.

7(a) Treasury Management Mid-Year Report 2021/22: (Pages 13 - 36)

Reference from Cabinet.

8. **Information Report - Invitation from Public Sector Audit Appointments to opt-in to external audits from 2023-24 to 2027-28** (Pages 37 - 44)  
Report of the Director of Finance and Assurance.
9. **Any Other Urgent Business**  
Which cannot otherwise be dealt with.
10. **Exclusion of the Press Public**  
To resolve that the press and public be excluded from the meeting for the following item of business, on the grounds that it involves the likely disclosure of confidential information in breach of an obligation of confidence, or of exempt information as defined under paragraph 3 in Part I of Schedule 12A to the Local Government Act 1972 9as amended):

| <u>Agenda Item No</u> | <u>Title</u>  | <u>Description of Exempt Information</u>  |
|-----------------------|---|---|
| 11.                   | Information Report – Q3 Corporate Risk Register 2021/22 | Information relating to the financial or business affairs of any particular person (including the authority holding that information) |

## **Agenda - Part II**

11. **Information Report - Q3 Corporate Risk Register 2021/22** (Pages 45 - 78)  
Report of the Director of Finance and Assurance.

### **\* Data Protection Act Notice**

The Council will record the meeting and will place the recording on the Council's website.

**[Note:** The questions and answers will not be reproduced in the minutes.]



# **Governance, Audit, Risk Management and Standards Committee**

## **Minutes**

### **30 November 2021**

**Present:**

**Chair:** Councillor David Perry

**Councillors:** Dean Gilligan Kanti Rabadia  
Kairul Kareema Marikar

**Joined virtually:** Philip Benjamin Antonio Weiss  
Amir Moshenson

**188. Attendance by Reserve Members**

**RESOLVED:** To note that there were no Reserve Members in attendance.

**189. Declarations of Interest**

**RESOLVED:** To note the declarations as published on the Council's website prior to the meeting and the following additional declaration made by Councillor Kairul Kareema Marikar during consideration of:

Agenda Item 11 – Statement of Account

Councillor Marikar declared an interest in that she had a care business. She would leave the Chamber if the interest became pecuniary.

**190. Minutes**

**RESOLVED:** That the minutes of the meeting held on 12 October 2021, be taken as read and signed as a correct record.

#### **191. Public Questions**

**RESOLVED:** To note that no public questions were received.

#### **192. Petitions**

**RESOLVED:** To note that no petitions had been received.

#### **193. Deputations**

**RESOLVED:** To note that no deputations were received at the meeting under the provisions of Committee Procedure Rule 16.

#### **194. References from Council and other Committees/Panels**

None received.

#### **195. Late Reports**

Members agreed to accept the late reports for the special circumstances and grounds of urgency set out in the supplemental agenda. However, the Chair and the Vice-Chair stressed the importance of such technical reports being submitted to the Committee on time and with the main agenda.

### **Resolved Items**

#### **196. Information Report - Audit Completion of Statement of Accounts 2019-20 - Annual Audit Letters**

The Committee received a report of the Director of Finance and Assurance, which set the Annual Audit Letters for the Council and Pension Fund issued by the Council's external auditor, Mazars LLP, for the financial year ended 31 March 2020 for consideration. The report also referred to the completion of the external audit for the financial year 2019-20.

An officer introduced the report and highlighted the key positive conclusions arising from the external auditor's work, which were as follows:

- an unqualified audit opinion and value for money conclusion;
- no audit recommendations issued.

The officer added that the Audit Letters would be replaced with Annual Audit Reports in the future.

The Chair welcomed Lucy Nutley (Director) from Mazars LLP, the Council's external auditor, to add to the introduction and respond to questions from Members. Lucy Nutley drew attention to the executive summaries set out in the enclosures to the report. Members noted the reports from Mazars and agreed that any questions relating to the Council's performance and delivery

on issues such as Regeneration ought to be considered under the Statement of Accounts, Minute 199 refers.

**RESOLVED:** That the report be noted.

#### **197. Annual Governance Statement 2020/21**

The Committee received a report of the Director of Finance and Assurance, which set out the Head of Internal Audit's Final Audit Opinion and the Annual Governance Statement (AGS) for 2020/21.

The Head of Internal Audit and Corporate Anti-Fraud introduced the report reminded Members that they had received a draft ASG in July 2021. The Head drew Members' attention to the governance issues that she considered to be of particular significance:

- the Depot Redevelopment Project, which was no longer considered to be a significant governance gap; details of which were set out on page 35 of the main agenda;
- an emerging issue, allegations of fraud and corruption, which was currently the subject of a criminal investigation and which had been covered in Part II (confidential) verbal briefing at the last meeting. Members were informed that the outcome of the investigation would be reported to the Committee in due course.

The Chair welcomed the transparency and the challenges faced by the Council but highlighted the need to recognise and applaud the positive elements within the report.

**RESOLVED:** That

- (1) the Head of Internal Audit's final audit opinion 2020/21 be noted;
- (2) having reviewed the Annual Governance Statement 2020/21 in line with the Committee's terms of reference, and confirmed that the Annual Governance Statement (AGS) properly reflected the risk environment and supporting assurances and legal and financial advice, taking into account internal audit's opinion on the overall adequacy and effectiveness of the Council's framework of governance, risk management and control; the Committee was satisfied and recommended it for approval by the Leader and Chief Executive.

#### **198. Information Report - Audit Progress Report**

The Committee received a report of the Director of Finance and Assurance, which included an appendix that provided an update on progress from Mazars LLP, Council's external auditor, on the delivery of their responsibilities and highlighted the potential risk of there being a significant weakness in Value for Money (VFM) arrangements relating to an alleged identified fraud.

Lucy Nutley (Director) from Mazars LLP informed Members that the new Code of Audit Practice issued by the National Audit Office had changed the work that auditors were previously required to do on the Council's arrangements to deliver VFM, details of which were set out on page 43 of the supplemental agenda. She added that the related reporting arrangements had also changed in that any weaknesses in VFM arrangements had to be reported to those charged with governance, which was the GARMS Committee.

Lucy Nutley reported on a potential significant weakness in arrangements in an area in relation to the operation of internal controls and the achievement of value for money. A further report, the Auditor's Annual Report, was intended to be submitted to the April 2022 meeting of the Committee, which would contain this risk and set out the need for any further recommendations to be issued or confirm that appropriate mitigating actions had been taken by the Council.

Lucy Nutley responded to questions from Members as follows:

- the work carried out by Mazars LLP would include a review of the findings and recommendations of the internal audit, including the progress made by management in their implementation. Additionally, consideration would be given to the findings and recommendations of the Independent Review, commissioned by the Council's Chief Executive, including the progress made by management in their implementation of any recommendations;
- the report in April 2022 would detail the outcome in relation to this risk but she pointed out that the risk may continue until 2022/23;

The Chair stated that the Council's Internal Audit team were involved in the review of the risk and that Councillors would also be involved. The Head of Internal Audit and Corporate Anti-Fraud reported that information could not be made public until the Police had concluded their investigations into the allegations but that the work being carried out by her team and the Independent Review would continue to be reported to the Committee when possible.

**RESOLVED:** That the report be noted.

## **199. Statement of Accounts 2020-21**

The Committee received a report of the Director of Finance and Assurance, setting out the audited Statement of Accounts for 2020-21 which were subject to the issue of the audit opinion.

Lucy Nutley (Director) from Mazars LLP, the Council's external auditor who had prepared detailed reports on matters arising from the audit of the Statement of Accounts and the Pension Fund Annual Report, drew Members' attention to the Executive Summary on page 241 of the supplemental agenda and outlined the key messages therein, including that their opinion on the financial statements was subject to further work being carried out, but it was

anticipated to be an unqualified opinion on the financial statements. She hoped that the financial statements would be signed off in December 2021.

Members' attention was also drawn to the significant audit risks identified, which were, in the following areas:

- management override of controls;
- revenue recognition;
- property plant and equipment valuation, including investment property (noting that a material valuation uncertainty had been recorded on the valuation of investment property of a specialised nature);
- defined benefit pension liability valuation (noting that a material valuation uncertainty had been recorded on the valuation of the Council's share in the Pension Fund assets);
- grants accounting.

Lucy Nutley referred to supplemental agenda pages 261 onwards, including appendices A and C, and identified areas including those where Mazars had been satisfied with the Council's management responses to the internal control recommendations and the summary of misstatements. Together with Stuart Frith (Manager – Mazars LLP), she responded to Members' questions as follows:

- the valuation of investment property assets and holdings held in the Council's Pension Fund in areas such as retail and leisure and where the impact of Covid-19 was ongoing would show the "emphasis of matter" within the audit opinion, due to the fact a material valuation uncertainty had been recognised in the formal valuation;
- the Pension Fund accounts were set out separately. Approximately 80% of the Pension Fund related to current and former Harrow employees.
- the changes in financial assumptions of approximately £260m, used in calculating the defined benefit pension liability, as set out on page 121 of the supplemental agenda, was due to a change in assumptions applied compared to in the previous year. All assumptions applied had been reviewed and compared to the national report issued by Pricewaterhouse Coopers LLP. The change arose from a number of factors, all of which would increase the liability of the Council: increases in overall life expectancy, salaries and pensions. The figure of £260m was calculated by the Pension Fund's actuary in accordance with the relevant code of practice. Mazars had assessed the independence of both the actuary (appointed by the National Audit Office) and Pricewaterhouse Coopers LLP and the assumptions made were appropriate;

- in respect of IT Security, there had been no indication of any untoward access of IT by former employees but that the ability to do so had been present. All Internal Audit Plans would cover any issues with the IT and extra testing would be carried out to test for potential breaches.

The Director of Finance and Assurance also responded to a question on the lessons learnt as a result of the Covid-19 pandemic which might be applied in any future potential waves, both in terms of the production of the accounts and the overall impact on the Council and its finances, including the making of policy decisions. The Council had faced a challenging financial budget in 2020/21 but had delivered a balanced budget. Similar principles were being applied this year (2021/22) and it was anticipated to be 'business as usual'. A small amount of Covid funding had been received from the government compared to the previous year. However, the Council was mindful that no such funding would be received next year (2022/23).

The Chair outlined the role of the Committee and the need for a robust challenge in both the Council's finances and the work carried out by its external auditors. Lucy Nutley added that good practices were shared amongst local authorities. She responded to additional questions from the Chair in regard to the Redmond Review and the implications the recommendations would have on the Council. She explained that whilst the recommendations had been accepted by the DLUHC (Department of Levelling Up, Housing and Communities), they were not required to be implemented yet and direction was awaited. The biggest change was the requirement for the external auditor to report to full Council.

In response to additional questions, the representatives from Mazars LLP

- undertook to provide a written response to all Members of the Committee in relation to the query on usable reserves of £159m and how these would be recovered if realised;
- stated that further information on risks as a result of the Covid-19 pandemic, regeneration aspirations of the Council and governance would be included in the report to April 2022 meeting of the Committee.

Members' attention was then drawn to the Executive Summary relating to the Harrow Pension Fund (year ended 31 March 2021), page 285 of the supplemental agenda referred, which set out the conclusions on the audit opinion, consistency report and wider powers. Members were advised of any significant findings as set out on pages 291 and 292 of the supplemental agenda and the summary of misstatements on page 297 of the agenda.

Stuart Frith and the Council's Director of Finance and Assurance responded to questions from the Committee in relation to the funding of the Pension Fund. For the purposes of IAS 19 (International Accounting Standard), the Fund was 70% funded and due to longevity and other reasons identified earlier, the deficit had increased. However, these were forecasts and the situation could change. The Director of Finance and Assurance advised Members that the Pension Fund was well funded and was monitored

quarterly. Provision had been made in the revenue budget to allow for contributions to any deficit in the Fund.

A further explanation was provided by an officer – the employer contributions were assessed by the actuary at each triennial valuation, and were calculated on an “ongoing funding basis” which reflected that the scheme was open to future accrual of pensions. On that basis, the scheme was currently 104% funded. IAS 19 used different assumptions, and assessed the extent to which the current pension liabilities were covered by the Fund’s investments at the date of the accounts. The different assumptions used in the two funding calculations were outlined on pages 227 to 229 of the supplemental agenda. The caveats that needed to be applied to the Fund were: future pay increases, inflation, number of staff employed and mortality/longevity.

On the question of the “emphasis of matter” in respect of the Pension Fund’s property investments, Stuart Frith added that Mazars LLP did not have direct access to the Pension Fund and information was requested from the Fund Managers. Mazars would rely on the Fund Manager’s independence and expertise and were satisfied with the Fund Manager and an emphasis of matter would be issued in line with expectations. Mazars would have brought any issues to the attention of the Committee, including the work of the Pension Fund Committee and the Pension Board. Control reports of the Fund Manager would be studied, including their management of Funds. Any issues would have been reported and brought to the attention of this Committee. An unqualified opinion should be expected.

The Chair requested that the Director of Finance and Assurance report back to the Corporate Strategy Board on the discussion of the Committee in respect of the report, including the scrutiny it had made, together with the positive delivery of numerous Council priorities/policy areas.

**RESOLVED:** That, having considered the draft Audit Completion Reports of the External Auditor on matters arising from the audit of the Statement of Accounts 2020-21 and the Pension Fund Annual Report 2020-21,

- (1). the audited Statement of Accounts 2020-21 be approved and the Chair be authorised to sign the accounts, subject to resolution 3 below;
- (2). the Pension Fund Annual Report 2020-21 be noted;
- (3). the Director of Finance and Assurance, following consultation with the Chair, be authorised to make any final amendments to the Statement of Accounts 2020-21 and the Pension Fund Annual Report 2020-21 arising from the external audit prior to the signing by the auditor;
- (4). the Summary Statement of Accounts 2019-20 be noted.

(Note: The meeting, having commenced at 6.31 pm, closed at 8.07 pm).

(Signed) Councillor David Perry  
Chair



**GOVERNANCE, AUDIT, RISK MANAGEMENT AND STANDARDS  
COMMITTEE – 25 JANUARY 2022**

**Reference from Cabinet – 9 December 2021**

**582. Treasury Management Mid-Year Report 2021/22**

**RESOLVED:** That

- (1) the Treasury Management Mid-Year Review for 2021/22, be noted; and
- (2) the report be referred to the Governance, Audit, Risk Management and Standards Committee for review.

**Reason for Decision:**

- a) To promote effective financial management and comply with regulations issued under the Local Government Act 2003, the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management, and the CIPFA Prudential Code for Capital Finance, along with meeting the requirements of the Council's Financial Regulations.
- b) To keep Members informed of Treasury Management activities and performance to date for 2021/22.

**For Consideration**

**Background Documents:**

Treasury Management Mid-Year Report 2021/22

**Contact Officer:**

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**Report for: Cabinet**

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|                                     |   |
|-------------------------------------|---|
| <b>Date of Meeting:</b>             | 9 <sup>th</sup> December 2021   |
| <b>Subject:</b>                     | Treasury Management Mid-Year Report 2021/22   |
| <b>Key Decision:</b>                | No  |
| <b>Responsible Officer:</b>         | Dawn Calvert, Director of Finance and Assurance   |
| <b>Portfolio Holder:</b>            | Councillor Natasha Proctor, Deputy Leader and Portfolio Holder for Finance and Resources              |
| <b>Exempt:</b>                      | No  |
| <b>Decision subject to Call-in:</b> | No  |
| <b>Wards affected:</b>              | All wards   |
| <b>Enclosures:</b>                  | Appendix 1 Link Group Economic Commentary<br>Appendix 2 Borrowing and Investment Rate Summary 2021/22 |

## **Section 1 – Summary and Recommendations**

This report provides a Mid-Year Review of the Council's Treasury Management activities in 2021/22 in compliance with the CIPFA Treasury Management Code of Practice.

### **Recommendations:**

Cabinet is requested to:

1. Note the Treasury Management Mid-Year Review for 2021/22.
2. Refer this report to the Governance, Audit, Risk Management and Standards Committee for review.

### **Reason: (for recommendations)**

- a) To promote effective financial management and comply with regulations issued under the Local Government Act 2003, the CIPFA Code of Practice on Treasury Management, and the CIPFA Prudential Code for Capital Finance, along with meeting the requirements of the Council's Financial Regulations.
- b) To keep Members informed of Treasury Management activities and performance to date for 2021/22.

## **Section 2 – Report**

### **1.0. Introduction**

1.1. The purpose of this report is to update Members with the Council's Treasury Management activity in 2021/22, presenting performance to 30<sup>th</sup> September 2021 in accordance with the Council's Treasury Management Practices and in compliance with the CIPFA Treasury Management Code of Practice. The Council has complied with all elements of the Treasury Management Strategy Statement (TMSS) as the treasury management function.

1.2. Treasury management comprises:

- Managing the Council's borrowing to ensure funding of the Council's current and future Capital Programme is at optimal cost;
- Investing surplus cash balances arising from the day-to-day operations of the Council to obtain an optimal return while ensuring security of capital and liquidity.

1.3. The annual revenue budget includes the revenue costs that flow from capital financing decisions. Under the CIPFA Treasury Management Code of Practice and the CIPFA Prudential Code, increases in capital expenditure should be

limited to levels whereby increases in interest charges and running costs are affordable within the Council's revenue account.

- 1.4. The Council regards the successful identification, monitoring and control of risk to be 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 to ensure the security and liquidity of the Council's treasury investments.
- 1.5. The Council recognises 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 the CIPFA Treasury Management Code of Practice.

## 2.0. Reporting Requirements

- 2.1. The Council and/or Cabinet are required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.
- 2.2. **Treasury Management Strategy Statement Report** – The first, and most important report is presented to the Council in February and covers:
  - The Treasury Management Strategy Statement (TMSS), which details how the investments and borrowings for capital expenditure are to be organised, including Treasury Limits and Prudential Indicators.
  - The Annual Investment Strategy which forms part of the TMSS, (the parameters on how investments are to be managed).
  - the MRP Policy (how capital expenditure is charged to revenue over time).

**The 2021/22 TMSS was presented to Council on 25 February 2021.**

- 2.3. **Mid-Year Review Report** – This is presented to Cabinet in December/January and updates Members on the progress of the Capital Programme, reporting on Prudential Indicators to give assurance that the treasury management function is operating within the Treasury Limits and Prudential Indicators set out in the TMSS.

**This report fulfills the requirements of the the Mid-Year Review for 2021/22.**

- 2.4. **Treasury Management Outturn Report** – This is typically presented to Cabinet in June/July and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the TMSS and Mid-Year Reports.
- 2.5. **Scrutiny** – The above reports are required to be adequately scrutinised, normally before being recommended to Cabinet/Council, with the role being undertaken by the Governance, Audit, Risk Management and Standards Committee (GARMS). The Council has complied with the CIPFA Treasury

Management Code of Practice to the extent that all Treasury Management reports have been scrutinised through the efficient conduct of the Council's business may require consideration by GARMS subsequent to consideration by Cabinet/Council.

- 2.6. The Council has delegated responsibility for the implementation and regular monitoring of its treasury management policies and practices to the Section 151 Officer. The Section 151 Officer chairs the Treasury Management Group (TMG), which monitors the treasury management activity and market conditions monthly.

### **3.0. Options considered**

- 3.1. The report is in accordance with the reporting requirements of the CIPFA Treasury Management Code of Practice.

### **4.0. Treasury Management Strategy Statement and Annual Investment Strategy Update**

- 4.1. The Treasury Management Strategy Statement, (TMSS), for 2021/22 was approved by Council on 25 February 2021.
- 4.2. There are no policy changes proposed to the TMSS approved for 2021/22; the details in this report update the position in the light of the updated economic environment, budgetary changes and revised capital programme outturn forecast contained in the 2021/22 Q2 Capital Budget Monitoring Report also presented at this meeting.

### **5.0. GLA Group Investment Syndicate**

- 5.1. The Cabinet report dated 15th July 2021, set out a recommendation that the Council becomes a participant in the shared service arrangement operated by the Greater London Authority (GLA) for the provision of treasury management services. This will include the Council transferring its investment balances into the GLA Group Investment Syndicate (GIS).
- 5.2. Work remains ongoing in respect of finalising the associated legal agreement to conclude negotiations to the satisfaction of the Director of Finance and Assurance in consultation with the Portfolio Holder for Finance and Resources together with the Director of Legal and Governance.
- 5.3. It is anticipated that this agreement may be in place for 2022/23.

### **6.0. CIPFA Treasury Management Code of Practice and Prudential Code consultations**

- 6.1. CIPFA are currently consulting on revisions to the Treasury Management Code of Practice and Prudential Code. The second stage of the consultation process closed on the 16 November 2021 and we are awaiting the outcome of the consultation. CIPFA have indicated that due to the timing of the

consultations the introduction of changes from the revised Codes will be in the form of a soft launch with full implementation expected from 2023/24.

## 7.0. Compliance with Prudential Indicators

- 7.1. It is a statutory duty for the Council to determine and keep under review its affordable borrowing limits. The Council has operated within the Treasury and Prudential Indicators set out in the Council's Treasury Management Strategy Statement for 2021/22 during the half year ended 30 September 2020 (and up to 29 November 2021 at the point this report was despatched).
- 7.2. All treasury management operations have been conducted in full compliance with the Council's Treasury Management Practices.

### Prudential Indicator for Capital Expenditure

- 7.3. The Council's Capital Programme is a key driver of Treasury Management activity. The output of the Capital Programme is reflected in the statutory prudential indicators, which are designed to provide Member's with an overview of the impact of the capital expenditure plans and ensure that these remain prudent, affordable and sustainable.
- 7.4. Table 1 shows the revised estimates for capital expenditure to reflect updates to the 2021/22 capital programme since the capital programme was agreed as part of the 2021/22 Budget.

Table 1

| <b>Capital expenditure<br/>£'000</b> | <b>2021/22<br/>Original Estimate</b> | <b>2021/22<br/>Revised Estimate</b> |
|--------------------------------------|--------------------------------------|-------------------------------------|
| - Resources and Commercial           | 14,731                               | 14,583                              |
| - People's                           | 22,803                               | 11,528                              |
| - Community                          | 48,092                               | 62,716                              |
| <b>General Fund</b>                  | <b>85,626</b>                        | <b>88,827</b>                       |
| <b>HRA</b>                           | <b>90,823</b>                        | <b>99,595</b>                       |
| <b>Total</b>                         | <b>176,449</b>                       | <b>188,422</b>                      |

- 7.5. The 2021/22 Q2 Capital Budget Monitoring Report provides further details of the updated forecast outturn position.

### Changes to the Financing of the Capital Programme

- 7.6. Table 2 illustrates how the Council's capital expenditure plans (table 1) will be funded. The net financing need for the year increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

Table 2

| Financing of capital expenditure<br>£'000 | 2021/22<br>Original Estimate | 2021/22<br>Revised Estimate |
|---|------------------------------|-----------------------------|
| <b>General Fund</b>                       |                              |                             |
| Capital Receipts                          | 2,641                        |                             |
| Capital Grants                            | 27,362                       | 17,365                      |
| BCiL                                      | 4,027                        | 4,085                       |
| NCiL                                      | 500                          | 588                         |
| Section 106                               |                              | 1,091                       |
| Revenue                                   |                              | 425                         |
| <b>External Funding</b>                   | <b>34,530</b>                | <b>23,554</b>               |
| <b>Net financing need for year (GF)</b>   | <b>51,096</b>                | <b>65,273</b>               |
| <b>HRA</b>                                |                              |                             |
| Capital Receipts                          | 7,848                        | 13,727                      |
| Capital Grants                            | 21,488                       | 17,997                      |
| Section 106                               | 3,165                        | 3,020                       |
| Revenue                                   | 12,143                       | 12,950                      |
| <b>External Funding</b>                   | <b>44,644</b>                | <b>47,694</b>               |
| <b>Net financing need for year (HRA)</b>  | <b>46,179</b>                | <b>51,901</b>               |
|   |                              |                             |
| <b>Total net financing need for year</b>  | <b>97,274</b>                | <b>117,174</b>              |

### Capital Financing Requirement

- 7.7. The CFR is the total historic outstanding capital expenditure incurred by the Council, which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any new capital expenditure, which has not immediately been paid for, will increase the CFR. The Council makes an annual charge to the revenue budget for the repayment of its debt liability, the Minimum Revenue Provision, which acts to reduce the CFR and charge prudential borrowing to the General Fund over time.
- 7.8. The Authority's CFR at 31 March 2021 was £573m (GF £422m/HRA £151m). Table 3 reflects the latest projections for the CFR based on the forecast outturn from the 2021/22 Q2 Capital Budget Monitoring Report, summarised in tables 1 and 2, and the Minimum Revenue Provision included within the 2021/22 Revenue Budget.

Table 3

| <b>Capital Financing Requirement<br/>£'000</b> | <b>2021/22<br/>Original Estimate</b> | <b>2021/22<br/>Revised Estimate</b> |
|--|--------------------------------------|-------------------------------------|
| CFR – General Fund                             | 467,891                              | 461,913                             |
| CFR – HRA                                      | 198,224                              | 202,575                             |
| <b>Total CFR</b>                               | <b>666,115</b>                       | <b>664,488</b>                      |
| <b>Movement in CFR</b>                         | <b>71,721</b>                        | <b>91,621</b>                       |

| <b>Movement in CFR represented by</b>      |               |               |
|--|---------------|---------------|
| Net financing need for the year (table 2)  | 97,274        | 117,174       |
| Less MRP/VRP and other financing movements | -25,553       | -25,553       |
| <b>Movement in CFR</b>                     | <b>71,721</b> | <b>91,621</b> |

### **Authorised Limit and Operational Boundary**

- 7.9. No changes have been proposed to the Council's Operational Boundary and Authorised Limit which were approved as part of the 2021/22 TMSS on 25 February 2021.

#### Operational Boundary

- 7.10. This limit is based on the Council's programme for capital expenditure, Capital Financing Requirement and cash flow needs for the year. It is the limit beyond which external debt is not normally expected to exceed.

Table 4

| <b>Operational boundary £'000</b> | <b>2021/22</b> |
|-----------------------------------|----------------|
| Borrowing                         | 666,115        |
| Other long term liabilities       | 17,370         |
| <b>Total</b>                      | <b>683,485</b> |

#### Authorised Limit

- 7.11. This is a key prudential indicator and represents a control on the maximum level of borrowing. This represents a legal limit beyond which external debt is prohibited, and this limit needs to be set or revised by full Council.
- 7.12. It is the statutory limit determined under section 3(1) of the Local Government Act 2003. Under the Act, the Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

Table 5

| <b>Authorised limit £'000</b> | <b>2021/22</b> |
|-------------------------------|----------------|
| Borrowing                     | 696,115        |
| Other long term liabilities   | 28,520         |
| <b>Total</b>                  | <b>724,635</b> |

## 8.0. Economic Update

- 8.1. The Monetary Policy Committee (MPC) on the 4<sup>th</sup> November voted 7-2 to leave Bank Rate unchanged at 0.10% with two members voting for an increase to 0.25% and made no changes to its programme of quantitative easing purchases due to finish by the end of this year at a total of £895bn by a vote of 6-3.
- 8.2. After the Governor and other MPC members had made speeches prior to the November MPC meeting in which they stressed concerns over inflation, (the Bank is now forecasting inflation to reach 5% in April when the next round of capped gas prices will go up), thus reinforcing their strong message from the September MPC meeting, financial markets had confidently built in an expectation that Bank Rate would go up from 0.10% to 0.25% in November.
- 8.3. While the Bank refrained from raising rates at the November meeting, the MPC did comment, however, that Bank Rate would have to go up in the short term. It is, therefore, relatively evenly balanced as to whether Bank Rate will be increased in December, February or May. Much will depend on how the statistical releases for the labour market after the end of furlough on 30<sup>th</sup> September 2021 turn out when published.
- 8.4. Over the next year the MPC will be doing a delicate balancing act of weighing combating inflation being higher for longer against growth being held back by significant headwinds. Those headwinds are due to supply shortages (pushing prices up and holding back production directly), labour shortages, surging fuel prices and tax increases. However, those headwinds could potentially be offset – at least partially - by consumers spending at least part of the £160bn+ of “excess savings” accumulated during the pandemic. Conversely, there is also the possibility that people may be content to hold onto elevated savings and investments and, therefore, not support the economic recovery to the extent that the MPC may forecast.
- 8.5. The MPC pointedly chose to reaffirm its commitment to the 2% inflation target in its statement after the MPC meeting in September yet at its August meeting it had emphasised a willingness to look through inflation overshooting the target for limited periods to ensure that inflation was ‘sustainably over 2%’. On balance, once this winter is over and world demand for gas reduces - so that gas and electricity prices fall back - and once supply shortages of other goods are addressed, the MPC is forecasting that inflation would return to just under the 2% target within 3 years.

- 8.6. The MPC's forward guidance on its intended monetary policy on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows: -
1. Raising Bank Rate as "the active instrument in most circumstances".
  2. Raising Bank Rate to 0.50% before starting on reducing its holdings.
  3. Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
  4. Once Bank Rate had risen to at least 1%, it would start selling its holdings
- 8.7. Since the start of 2021, there has been volatility in gilt yields, and hence PWLB rates. During September, gilt yields from 5 – 50 years rose steadily and after the hawkish tone of the MPC's minutes on 23rd September. Gilt yields then fell sharply after the Budget on 27th October cancelled nearly all gilt sales until the end of the financial year. Forecasts from Link Group, the Councils treasury advisor show a steady, but slow, rise in both Bank Rate and gilt yields during the forecast period to March 2025.

### Interest Rate Forecast

- 8.8. The Council's treasury advisor, Link Group, provided the following forecasts on 8th November 2021 (PWLB rates are based on PWLB Certainty Rates, which are gilt yields plus 80bps):

| Link Group Interest Rate View |        | 8.11.21 |        |        |        |        |        |        |        |        |        |        |        |        |
|-------------------------------|--------|---------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|                               | Dec-21 | Mar-22  | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 |
| BANK RATE                     | 0.25   | 0.25    | 0.50   | 0.50   | 0.50   | 0.75   | 0.75   | 0.75   | 0.75   | 1.00   | 1.00   | 1.00   | 1.00   | 1.25   |
| 3 month ave earnings          | 0.30   | 0.40    | 0.50   | 0.50   | 0.50   | 0.60   | 0.80   | 0.90   | 1.00   | 1.00   | 1.00   | 1.00   | 1.00   | 1.00   |
| 6 month ave earnings          | 0.40   | 0.50    | 0.60   | 0.60   | 0.70   | 0.80   | 0.90   | 1.00   | 1.10   | 1.10   | 1.10   | 1.10   | 1.10   | 1.10   |
| 12 month ave earnings         | 0.50   | 0.60    | 0.70   | 0.70   | 0.80   | 0.90   | 1.00   | 1.10   | 1.20   | 1.20   | 1.20   | 1.20   | 1.20   | 1.20   |
| 5 yr PWLB                     | 1.50   | 1.50    | 1.60   | 1.60   | 1.70   | 1.70   | 1.70   | 1.80   | 1.80   | 1.80   | 1.90   | 1.90   | 2.00   | 2.00   |
| 10 yr PWLB                    | 1.80   | 1.90    | 1.90   | 2.00   | 2.00   | 2.10   | 2.10   | 2.20   | 2.20   | 2.20   | 2.30   | 2.30   | 2.30   | 2.40   |
| 25 yr PWLB                    | 2.10   | 2.20    | 2.30   | 2.40   | 2.40   | 2.40   | 2.50   | 2.50   | 2.60   | 2.60   | 2.60   | 2.60   | 2.70   | 2.70   |
| 50 yr PWLB                    | 1.90   | 2.00    | 2.10   | 2.20   | 2.20   | 2.20   | 2.30   | 2.30   | 2.40   | 2.40   | 2.40   | 2.40   | 2.50   | 2.50   |

## 9.0. Treasury Position as at 30 September 2021

### Investments

- 9.1. In accordance with the CIPFA Treasury Management Code of Practice and MHCLG Investment Guidance, the TMSS sets out the Council's investment priorities as being:
- Security of capital
  - Liquidity
  - Yield
- 9.2. It is now impossible to earn the level of interest rates commonly seen in previous decades as short-term money market investment rates have continued to remain low following the cut in Bank Rate to 0.10% in March 2020. After the MPC meeting on 24th September 2021 6 month to 12 month deposit rates rose in anticipation of Bank Rate going up in 2022, and while the MPC didn't raise Bank Rate in November in line with market expectations, it has continued to price in an increase which have impacted yields for durations in all but the short term liquidity periods, albeit marginally. Given this low starting point and the fact that Bank Rate is still only forecast to rise incrementally

through to March 2025 means that investment returns are expected to remain low for the foreseeable future.

Table 6

| Investment Portfolio<br>£'000 | 31-Mar-21 |                  |                     | 30-Sep-21 |                  |                     |
|-------------------------------|-----------|------------------|---------------------|-----------|------------------|---------------------|
|                               | Principal | Average Rate (%) | Average Life (days) | Principal | Average Rate (%) | Average Life (days) |
| - MMFs                        | 1,616     | 0.00%            | 1                   | 1,616     | 0.01%            | 1                   |
| - Banks                       | 80,838    | 0.01%            | 4                   | 118,115   | 0.01%            | 4                   |
| Total Investments             | 82,454    | 0.01%            | 4                   | 119,731   | 0.01%            | 4                   |

9.3. The Council held £120m of investments as at 30 September 2021 compared with £82m at 31 March 2021. The portfolio remains highly liquid with the yield reflecting the current market for liquid investments. Cashflow forecasting has been challenging during 2021/22 due to the continued response to the pandemic and the impact this has had on the Authority along with the Council's continued role within that response. The internal borrowing strategy of the Authority, focusing on minimising the net cost of borrowing, also prevents longer term investment with a consequential impact on investment return.

9.4. The Council's investment income budget for 2021/22 is £1.256m and the forecast outturn is £1.2m. This includes income from the £15m loan to the West London Waste Authority which the Council approved in July 2013 to finance the cost of a new energy waste plant. The term of the loan is 25 years at an interest rate of 7.604% on a reducing balance basis. The loan balance at the 31 March 2021 was £15.8m which includes interest accrued to date.

9.5. During the period cash investments have been held with Deutsche and Fidelity Money Market Funds, Lloyds, Royal Bank of Scotland PLC, and Svenska Handelsbanken. Counterparty use has been consistent with previous years and in accordance with the credit criteria set out in the TMSS. Officers can confirm that the approved limits within the Annual Investment Strategy have not been breached to the period of 29th November 2021.

9.6. There are no changes proposed to the Council's Investment Counterparty Criteria approved in the 2021/22 TMSS.

### **Borrowing**

9.7. The Council continues to run an internal borrowing strategy with a borrowing portfolio of £422m (excluding £17.6m of PFI and Finance Lease Liabilities) below the actual CFR of £573m as at 31 March 2021 and the revised estimate of the CFR for 31 March 2022 of £664m, based on the forecast outturn for the from the 2021/22 Q2 Capital Budget Monitoring Report.

9.8. The Authority's current borrowing portfolio remains unchanged from 31 March 2021, with no new borrowing undertaken in 2021/22 to date up to 29 November 2021.

9.9. The forecast outturn on borrowing costs is £14.929m, a favourable variance of £4.008m on the budget of £18.937m, reflecting the continued internal borrowing strategy adopted by the Authority.

Table 7

| Borrowing Portfolio<br>£'000 | 31-Mar-21 |                  |                    | 30-Sep-21 |                  |                    |
|------------------------------|-----------|------------------|--------------------|-----------|------------------|--------------------|
|                              | Principal | Average Rate (%) | Average Life (yrs) | Principal | Average Rate (%) | Average Life (yrs) |
| - PWLB                       | 348,461   | 3.45%            | 36.0               | 348,461   | 3.45%            | 35.5               |
| - Market                     | 73,800    | 3.53%            | 41.7               | 73,800    | 3.53%            | 41.2               |
| Total borrowing              | 422,261   | 3.46%            | 37.0               | 422,261   | 3.46%            | 36.5               |

9.10. The Director of Finance will continue to keep borrowing decisions under review.

9.11. The maturity structure of the debt portfolio remained within the Prudential Indicator limits set as part of the 2021/22 Treasury Management Strategy. The maturity structure table (8) below includes one Lenders Option Borrowers Option (LOBO) market loan at its next call date, which is the earliest date the lender can require repayment.

Table 8

| Maturity structure of borrowing 2021/22 | Lower Limit | Upper Limit | Actual 31.03.21 | Actual 30.09.21 |
|---|-------------|-------------|-----------------|-----------------|
| Under 12 months                         | 0%          | 40%         | 5%              | 5%              |
| 12 months to 2 years                    | 0%          | 30%         | 1%              | 1%              |
| 2 years to 5 years                      | 0%          | 30%         | 0%              | 0%              |
| 5 years to 10 years                     | 0%          | 40%         | 5%              | 5%              |
| 10 years and above                      | 30%         | 100%        | 89%             | 89%             |

## 10.0. Implications of the Recommendation

### 11.0. Risk Management Implications

This report is for noting and Cabinet are not being asked to make any decisions hence there are no direct risk management implications to this report.

### 12.0. Procurement Implications

There are no procurement implications arising from this report.

### 13.0. Legal Implications

The Local Government Act 2003 requires the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to

ensure that the Council's capital investment plans are affordable, prudent and sustainable. These are contained within this report.

The Act, accompanying statutory guidance and Codes of Practice referred to through capital financing regulations requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy. This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments. This report assists the Council in fulfilling its statutory obligation under the Local Government Act 2003 to monitor its borrowing and investment activities.

#### **14.0. Financial Implications**

In addition to supporting the Council's revenue and capital programmes the Treasury Management interest budget is an important part of the revenue budget. Any savings achieved, or overspends incurred, have a direct impact on the financial performance of the budget.

#### **15.0. Equalities implications / Public Sector Equality Duty**

There is no direct equalities impact.

#### **16.0. Council Priorities**

This report deals with the Treasury Management Strategy which plays a significant part in supporting the delivery of all the Council's corporate priorities.

### **Section 3 - Statutory Officer Clearance**

**Statutory Officer: Dawn Calvert**

Chief Financial Officer

**Date: 30/11/2021**

**Statutory Officer: Jessica Farmer**

Signed by the Monitoring Officer

**Date: 1/12/2021**

**Chief Officer: Charlie Stewart**

Signed off by the Corporate Director

**Date: 30/11/2021**

**Head of Procurement: Nimesh Mehta**

Signed off by the Head of Procurement

**Date: 30/11/2021**

**Head of Internal Audit: Susan Dixon**

Signed off by the Head of Internal Audit

**Date: 26/11/2021**

## **Mandatory Checks**

**Ward Councillors notified: NO, as it impacts on all Wards**

**EqlA carried out: NO – report is for information and not decision making.**

## **Section 4 - Contact Details and Background Papers**

**Contact:** Dawn Calvert – Director of Finance & Assurance,  
[dawn.calvert@harrow.gov.uk](mailto:dawn.calvert@harrow.gov.uk),

**Background Papers:**

**Call-in waived by the Chair of Overview and Scrutiny Committee**

**NO**

## **Appendix 1 Link Group Economic Commentary**

### **MPC meeting 4<sup>th</sup> November 2021**

- 1.0. The Monetary Policy Committee (MPC) voted 7-2 to leave Bank Rate unchanged at 0.10% with two members voting for an increase to 0.25% and made no changes to its programme of quantitative easing purchases due to finish by the end of this year at a total of £895bn by a vote of 6-3.
- 1.1. After the Governor and other MPC members had made speeches prior to the MPC meeting in which they stressed concerns over inflation, (the Bank is now forecasting inflation to reach 5% in April when the next round of capped gas prices will go up), thus reinforcing the strong message from the September MPC meeting, financial markets had confidently built in an expectation that Bank Rate would go up from 0.10% to 0.25% at this meeting. However, these were not messages that the MPC would definitely increase Bank Rate at the first upcoming MPC meeting as no MPC member can commit the MPC to make that decision ahead of their discussions at the time. The MPC did comment, however, that Bank Rate would have to go up in the short term. It is, therefore, relatively evenly balanced as to whether Bank rate will be increased in December, February or May. Much will depend on how the statistical releases for the labour market after the end of furlough on 30th September 2021 turn out.
- 1.2. Information available at the December MPC meeting will be helpful in forming a picture but not conclusive, so this could cause a delay until the February meeting. At the MPC's meeting in February it will only have available the employment figures for November: to get a clearer picture of employment trends, it would, therefore, need to wait until the May meeting (although it also meets in March) when it would have data up until February. At its May meeting, it will also have a clearer understanding of the likely peak of inflation expected around that time. If the statistics show the labour market coping well during the next six months, then it is likely there will be two increases in these three meetings.
- 1.3. Over the next year the MPC will be doing a delicate balancing act of weighing combating inflation being higher for longer against growth being held back by significant headwinds. Those headwinds are due to supply shortages (pushing prices up and holding back production directly), labour shortages, surging fuel prices and tax increases. However, those headwinds could potentially be offset – at least partially - by consumers spending at least part of the £160bn+ of “excess savings” accumulated during the pandemic. However, it is also possible that more affluent people may be content to hold onto elevated savings and investments and, therefore, not support the economic recovery to the extent that the MPC may forecast.
- 1.4. The latest forecasts by the Bank showed inflation under-shooting the 3 years ahead 2% target (1.95%), based on market expectations of Bank Rate hitting 1% in 2022. This implies that rates don't need to rise to market expectations of 1.0% by the end of next year.
- 1.5. It is worth recalling that the MPC pointedly chose to reaffirm its commitment to the 2% inflation target in its statement after the MPC meeting in September yet

at its August meeting it had emphasised a willingness to look through inflation overshooting the target for limited periods to ensure that inflation was 'sustainably over 2%'. On balance, once this winter is over and world demand for gas reduces - so that gas prices and electricity prices fall back - and once supply shortages of other goods are addressed, the MPC is forecasting that inflation would return to just under the 2% target.

- 1.6. The MPC's forward guidance on its intended monetary policy on raising Bank Rate versus selling (quantitative easing) holdings of bonds is as follows: -
  1. Raising Bank Rate as "the active instrument in most circumstances".
  2. Raising Bank Rate to 0.50% before starting on reducing its holdings.
  3. Once Bank Rate is at 0.50% it would stop reinvesting maturing gilts.
  4. Once Bank Rate had risen to at least 1%, it would start selling its holdings.
- 1.7. Gilt yields fell after the budget led to a reduction of £57.8bn in the forecast by the OBR for the deficit this year and a cancellation of nearly all gilt sales for the remainder of the financial year. There is a delicate balancing act in forecasting gilt yields and PWLB rates over the forecast period as when Bank Rate does increase to 0.50%, the Bank will stop reinvesting maturing gilts – but at a time when the size of gilt sales has just been slashed in the budget.

#### **Our forecasts for Bank Rate**

- 1.8. We are not expecting Bank Rate to go up fast after the initial rate rise; our view is that the supply potential of the economy has not taken a major hit during the pandemic: it should, therefore, be able to cope well with meeting demand after supply shortages subside over the next year, without causing inflation to remain elevated in the medium-term, or to inhibit inflation from falling back towards the MPC's 2% target after the spike up to 5%. We are therefore forecasting five increases in Bank Rate over the forecast period to March 2025, ending at 1.25%. However, we are far from confident that these forecasts will not need changing within a relatively short timeframe for the following reasons: -
  - There are increasing grounds for viewing the economic recovery as running out of steam during the summer and now into the autumn. This could lead into stagflation which would create a dilemma for the MPC as to whether to focus on combating inflation or supporting economic growth through keeping interest rates low.
  - Will some current key supply shortages spill over into causing economic activity in some sectors to take a significant hit?
  - Rising gas and electricity prices in October and next April and increases in other prices caused by supply shortages and increases in taxation next April, are already going to deflate consumer spending power without the MPC having to take any action on Bank Rate to cool inflation.
  - On the other hand, consumers are sitting on over £160bn of excess savings left over from the pandemic so when will they spend this sum, in part or in total?
  - It is estimated that there were around 1 million people who came off furlough at the end of September; how many of those would not have had jobs on 1st October and would therefore be available to fill labour shortages which are creating a major headache in many sectors of the economy? So, supply shortages which have been driving up both wages

and costs, could reduce significantly within the next six months or so and alleviate one of the MPC's key current concerns.

- We also recognise there could be further nasty surprises on the Covid front, on top of the flu season this winter, and even the possibility of another lockdown, which could all depress economic activity.
- If the UK invokes article 16 of the Brexit deal over the dislocation in trading arrangements with Northern Ireland, this has the potential to end up in a no deal Brexit.

1.9. In summary, with the high level of uncertainty prevailing on several different fronts, we expect to have to revise our forecasts again - in line with what the new news is.

1.10. It should also be borne in mind that Bank Rate being cut to 0.10% was an emergency measure to deal with the Covid crisis hitting the UK in March 2020. At any time, the MPC could decide to simply take away that final emergency cut from 0.25% to 0.10% on no other grounds than it being no longer being warranted and as a step forward in the return to normalisation. In addition, any Bank Rate under 1% is both highly unusual and highly supportive of economic growth.

#### **Our forecasts for PWLB rates and gilt and treasury yields**

1.11. Gilt yields. Since the start of 2021, we have seen a lot of volatility in gilt yields, and hence PWLB rates. During September, gilt yields from 5 – 50 years rose steadily and rose further after the hawkish tone of the MPC's minutes on 23rd September. Gilt yields then fell sharply after the Budget on 27th October cancelled nearly all gilt sales until the end of the financial year. Our forecasts show a steady, but slow, rise in both Bank Rate and gilt yields during the forecast period to March 2025.

1.12. While monetary policy in the UK will have a major impact on gilt yields, there is also a need to consider the potential impact that rising treasury yields in America could have on our gilt yields. As an average since 2011, there has been a 75% correlation between movements in US 10 year treasury yields and UK 10 year gilt yields. This is a significant UPWARD RISK exposure to our forecasts for longer term PWLB rates. However, gilt yields and treasury yields do not always move in unison.

1.13. US treasury yields. During the first part of the year, US President Biden's, and the Democratic party's, determination to push through a \$1.9trn (equivalent to 8.8% of GDP) fiscal boost for the US economy as a recovery package from the Covid pandemic was what unsettled financial markets. However, this was in addition to the \$900bn support package already passed in December 2020. This was then followed by additional Democratic ambition to spend \$1trn on infrastructure, which has just been passed by both houses, and an even larger sum on an American families plan over the next decade; this is still caught up in Democrat / Republican haggling. Financial markets were alarmed that all this stimulus was happening at a time when:

1. A fast vaccination programme has enabled a rapid opening up of the economy.
2. The economy has been growing strongly during 2021.

3. It started from a position of little spare capacity due to less severe lockdown measures than in many other countries.
  4. And the Fed was still providing stimulus through monthly QE purchases.
- 1.14. These factors could cause an excess of demand in the economy which could then unleash strong inflationary pressures. This could then force the Fed to take much earlier action to start increasing the Fed rate from near zero, despite their stated policy being to target average inflation.
- 1.15. At its 3rd November Fed meeting, the Fed decided to make a start on tapering QE purchases with the current \$80bn per month of Treasury securities to be trimmed by \$10bn in November and a further \$10bn in December. The \$40bn of MBS purchases per month will be trimmed by \$5bn in each month. If the run-down continued at that pace, the purchases would cease entirely next June but the Fed has reserved the ability to adjust purchases up or down. This met market expectations. These purchases are currently acting as downward pressure on treasury yields and so it would be expected that Treasury yields would rise as a consequence over the taper period, all other things being equal.
- 1.16. However, on the inflation front it was still insisting that the surge in inflation was "largely" transitory. In his post-meeting press conference, Chair Jerome Powell claimed that "the drivers of higher inflation have been predominantly connected to the dislocations caused by the pandemic" and argued that the Fed's tools cannot address supply constraints. However, with the Fed now placing major emphasis on its mandate for ensuring full employment, (besides containing inflation), at a time when employment has fallen by 5 million and 3 million have left the work force, resignations have surged due to the ease of getting better paid jobs and so wage pressures have built rapidly.
- 1.17. With wage growth at its strongest since the early 1980s, inflation expectations rising and signs of a breakout in cyclical price inflation, particularly rents, the FOMC's insistence that this is still just a temporary shock "related to the pandemic and the reopening of the economy", does raise doubts which could undermine market confidence in the Fed and lead to higher treasury yields.
- 1.18. As the US financial markets are, by far, the biggest financial markets in the world, any upward trend in treasury yields will invariably impact and influence financial markets in other countries. Inflationary pressures and erosion of surplus economic capacity look much stronger in the US compared to those in the UK, which would suggest that Fed rate increases eventually needed to suppress inflation, are likely to be faster and stronger than Bank Rate increases in the UK. This is likely to put upward pressure on treasury yields which could then spill over into putting upward pressure on UK gilt yields.
- 1.19. There are also possible downside risks from the huge sums of cash that the UK populace have saved during the pandemic; when savings accounts earn little interest, it is likely that some of this cash mountain could end up being invested in bonds and so push up demand for bonds and support their prices i.e., this would help to keep their yields down. How this will interplay with the Bank of England eventually getting round to not reinvesting maturing gilts and then later selling gilts, will be interesting to monitor.

**Globally, our views on economies are as follows: -**

- 1.20. **EU.** The slow role out of vaccines initially delayed economic recovery in early 2021 but the vaccination rate then picked up sharply. After a contraction of -0.3% in Q1, Q2 came in with strong growth of 2%. With Q3 at 2.2%, the EU recovery is nearly complete although countries dependent on tourism are lagging. Recent sharp increases in gas and electricity prices have increased overall inflationary pressures but the ECB is likely to see these as being only transitory after an initial burst through to around 4%, so is unlikely to be raising rates for a considerable time.
- 1.21. **German general election.** With the CDU/CSU and SPD both having won around 24-26% of the vote in the September general election, the composition of Germany's next coalition government may not be agreed by the end of 2021. An SPD-led coalition would probably pursue a slightly less restrictive fiscal policy, but any change of direction from a CDU/CSU led coalition government is likely to be small. However, with Angela Merkel standing down as Chancellor as soon as a coalition is formed, there will be a hole in overall EU leadership which will be difficult to fill.
- 1.22. **China.** After a concerted effort to get on top of the virus outbreak in Q1 2020, economic recovery was strong in the rest of the year; this enabled China to recover all the initial contraction. During 2020, policy makers both quashed the virus and implemented a programme of monetary and fiscal support that was particularly effective at stimulating short-term growth. At the same time, China's economy benefited from the shift towards online spending by consumers in developed markets. These factors helped to explain its comparative outperformance compared to western economies during 2020 and earlier in 2021. However, the pace of economic growth has now fallen back after this initial surge of recovery from the pandemic and China is now struggling to contain the spread of the Delta variant through sharp local lockdowns - which will also depress economic growth. There are also questions as to how effective Chinese vaccines are proving. Supply shortages, especially of coal for power generation, which is causing widespread power cuts to industry, are also having a sharp disruptive impact on the economy. In addition, recent regulatory actions motivated by a political agenda to channel activities into officially approved directions, are also likely to reduce the dynamism and long-term growth of the Chinese economy.
- 1.23. **Japan.** 2021 has been a patchy year in combating Covid. However, recent business surveys indicate that the economy is rebounding rapidly now that the bulk of the population is fully vaccinated and new virus cases have plunged. The Bank of Japan is continuing its very loose monetary policy but with little prospect of getting inflation back above 1% towards its target of 2%, any time soon: indeed, inflation was actually negative in July. New Prime Minister Kishida had promised a large fiscal stimulus package after the November general election which his party has now won.
- 1.24. **World growth.** World growth was in recession in 2020 but recovered during 2021. Inflation has been rising due to increases in gas and electricity prices, shipping costs and supply shortages. But these should subside during 2022.

**The balance of risks to the UK: -**

- 1.25. The overall balance of risks to economic growth in the UK is now to the downside, including residual risks from Covid and its variants - both domestically and their potential effects worldwide.

**Downside risks to current forecasts for UK gilt yields and PwLB rates include: -**

- 1.26. **Labour and supply shortages** prove more enduring and disruptive and depress economic activity.
- 1.27. **Mutations** of the virus render current vaccines ineffective, and tweaked vaccines to combat these mutations are delayed, resulting in further national lockdowns or severe regional restrictions.
- 1.28. **Bank of England** acts too quickly, or too far, over the next three years to raise Bank Rate and causes UK economic growth, and increases in inflation, to be weaker than we currently anticipate.
- 1.29. **The Government** acts too quickly to cut expenditure to balance the national budget.
- 1.30. **UK / EU trade arrangements** – if there was a major impact on trade flows and financial services due to complications or lack of co-operation in sorting out significant remaining issues.
- 1.31. A resurgence of the **Eurozone sovereign debt crisis**. The ECB has taken monetary policy action to support the bonds of EU states, with the positive impact most likely for “weaker” countries. In addition, the EU agreed a €750bn fiscal support package which has still to be disbursed. These actions will help shield weaker economic regions in the near-term. However, in the case of Italy in the longer term, the cost of the virus crisis has added to its already huge debt mountain and its slow economic growth will leave it vulnerable to markets returning to taking the view that its level of debt is unsupportable. There remains a sharp divide between northern EU countries favouring low debt to GDP and annual balanced budgets and southern countries who want to see jointly issued Eurobonds to finance economic recovery. This divide could undermine the unity of the EU in time to come.
- 1.32. Weak capitalisation of some **European banks**, which could be undermined further depending on the extent of credit losses resulting from the pandemic.
- 1.33. **German general election in September 2021**. Germany faces months of uncertainty while a new coalition government is cobbled together after the indecisive result of the election. Once that coalition is formed, Angela Merkel’s tenure as Chancellor will end and will leave a hole in overall EU leadership.
- 1.34. **Other minority EU governments**. Austria, Sweden, Spain, Portugal, Netherlands, Ireland and Belgium also have vulnerable minority governments dependent on coalitions which could prove fragile and, therein, impact market confidence/economic prospects and lead to increasing safe-haven flows.

1.35. **Geopolitical risks**, for example in China, Iran or North Korea, but also in Europe and Middle Eastern countries, which could lead to increasing safe-haven flows.

**Upside risks to current forecasts for UK gilt yields and PWLB rates: -**

1.36. The **Bank of England is too slow** in its pace and strength of increases in Bank Rate and, therefore, allows inflationary pressures to build up too strongly within the UK economy, which then necessitates a later rapid series of increases in Bank Rate faster than we currently expect.

1.37. Longer term US treasury yields rise strongly and pull gilt yields up higher than forecast.

**LINK GROUP FORECASTS**

1.38. We do not think that the MPC will embark on a series of increases in Bank Rate of more than 1.15% during the current and next three financial years as we do not expect inflation to return to being sustainably above 2% during this forecast period.

1.39. With unpredictable virus factors now being part of the forecasting environment, there is a risk that forecasts could be subject to significant revision during the next three years.

**Gilt yields and PWLB rates**

1.40. The general situation is for volatility in bond yields to endure as investor fears and confidence ebb and flow between favouring relatively more “risky” assets i.e., equities, or the safe haven of government bonds. The overall longer-run trend is for gilt yields and PWLB rates to rise.

1.41. There is likely to be exceptional volatility and unpredictability in respect of gilt yields and PWLB rates due to the following factors: -

- How strongly will changes in gilt yields be correlated to changes in US treasury yields?
- Will the Fed take action to counter increasing treasury yields if they rise beyond a yet unspecified level?
- Would the MPC act to counter increasing gilt yields if they rise beyond a yet unspecified level?
- How strong will inflationary pressures turn out to be in both the US and the UK and so impact treasury and gilt yields?
- How will central banks implement their new average or sustainable level inflation monetary policies?
- How well will central banks manage the withdrawal of QE purchases of their national bonds i.e., without causing a panic reaction in financial markets as happened in the “taper tantrums” in the US in 2013?
- Will exceptional volatility be focused on the short or long-end of the yield curve, or both?

1.42. Our forecasts are also predicated on an assumption that there is no break-up of the Eurozone or EU within our forecasting period, despite the major challenges that are looming up, and that there are no major ructions in

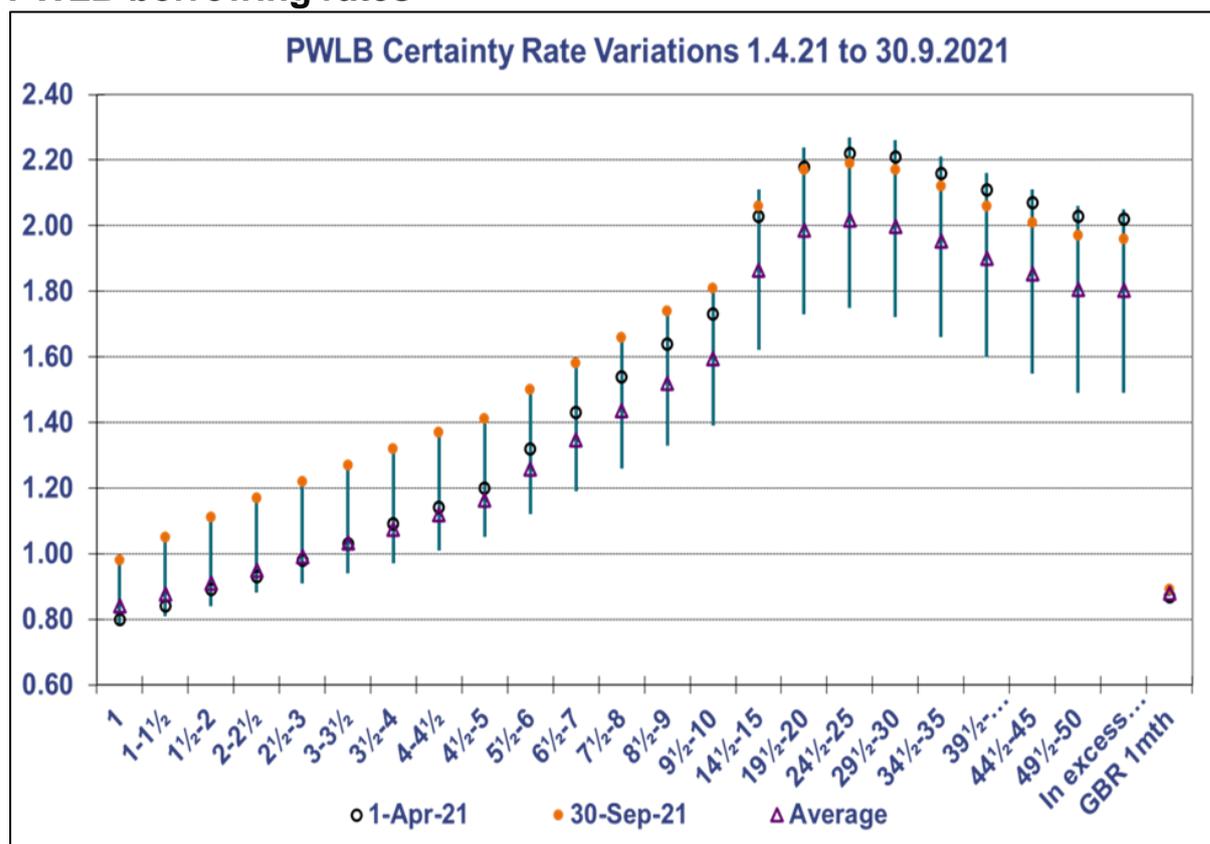
international relations, especially between the US and China / North Korea and Iran, which have a major impact on international trade and world GDP growth.

1.43. Our current and previous PWLB rate forecasts below are based on the Certainty Rate (the standard rate minus 20 bps) which has been accessible to most authorities since 1st November 2012.

| Link Group Interest Rate View 8.11.21 |        |        |        |        |        |        |        |        |        |        |        |        |        |        |
|---------------------------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
|                                       | Dec-21 | Mar-22 | Jun-22 | Sep-22 | Dec-22 | Mar-23 | Jun-23 | Sep-23 | Dec-23 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 |
| BANK RATE                             | 0.25   | 0.25   | 0.50   | 0.50   | 0.50   | 0.75   | 0.75   | 0.75   | 0.75   | 1.00   | 1.00   | 1.00   | 1.00   | 1.25   |
| 3 month ave earnings                  | 0.30   | 0.40   | 0.50   | 0.50   | 0.50   | 0.60   | 0.80   | 0.90   | 1.00   | 1.00   | 1.00   | 1.00   | 1.00   | 1.00   |
| 6 month ave earnings                  | 0.40   | 0.50   | 0.60   | 0.60   | 0.70   | 0.80   | 0.90   | 1.00   | 1.10   | 1.10   | 1.10   | 1.10   | 1.10   | 1.10   |
| 12 month ave earnings                 | 0.50   | 0.60   | 0.70   | 0.70   | 0.80   | 0.90   | 1.00   | 1.10   | 1.20   | 1.20   | 1.20   | 1.20   | 1.20   | 1.20   |
| 5 yr PWLB                             | 1.50   | 1.50   | 1.60   | 1.60   | 1.70   | 1.70   | 1.70   | 1.80   | 1.80   | 1.80   | 1.90   | 1.90   | 2.00   | 2.00   |
| 10 yr PWLB                            | 1.80   | 1.90   | 1.90   | 2.00   | 2.00   | 2.10   | 2.10   | 2.20   | 2.20   | 2.20   | 2.30   | 2.30   | 2.30   | 2.40   |
| 25 yr PWLB                            | 2.10   | 2.20   | 2.30   | 2.40   | 2.40   | 2.40   | 2.50   | 2.50   | 2.60   | 2.60   | 2.60   | 2.60   | 2.70   | 2.70   |
| 50 yr PWLB                            | 1.90   | 2.00   | 2.10   | 2.20   | 2.20   | 2.20   | 2.30   | 2.30   | 2.40   | 2.40   | 2.40   | 2.40   | 2.50   | 2.50   |

## Appendix 2 Borrowing and Investment Rate Summary 2021/22

### PWLB borrowing rates



|                | 1 Year     | 5 Year     | 10 Year    | 25 Year    | 50 Year    |
|----------------|------------|------------|------------|------------|------------|
| <b>Low</b>     | 0.78%      | 1.05%      | 1.39%      | 1.75%      | 1.49%      |
| <b>Date</b>    | 08/04/2021 | 08/07/2021 | 05/08/2021 | 17/08/2021 | 10/08/2021 |
| <b>High</b>    | 0.98%      | 1.42%      | 1.81%      | 2.27%      | 2.06%      |
| <b>Date</b>    | 24/09/2021 | 28/09/2021 | 28/09/2021 | 13/05/2021 | 13/05/2021 |
| <b>Average</b> | 0.84%      | 1.16%      | 1.60%      | 2.02%      | 1.81%      |
| <b>Spread</b>  | 0.20%      | 0.37%      | 0.42%      | 0.52%      | 0.57%      |

### Money market investment rates and forecasts 2021/22

|                  | Bank Rate  | 7 day      | 1 mth      | 3 mth      | 6 mth      | 12 mth     |
|------------------|------------|------------|------------|------------|------------|------------|
| <b>High</b>      | 0.10       | -0.08      | -0.07      | -0.04      | 0.05       | 0.25       |
| <b>High Date</b> | 01/04/2021 | 09/04/2021 | 06/07/2021 | 01/04/2021 | 30/09/2021 | 30/09/2021 |
| <b>Low</b>       | 0.10       | -0.09      | -0.08      | -0.07      | -0.04      | 0.03       |
| <b>Low Date</b>  | 01/04/2021 | 27/08/2021 | 26/04/2021 | 08/09/2021 | 27/07/2021 | 16/04/2021 |
| <b>Average</b>   | 0.10       | -0.08      | -0.07      | -0.05      | -0.02      | 0.07       |
| <b>Spread</b>    | 0.00       | 0.01       | 0.01       | 0.03       | 0.09       | 0.22       |



**Report for: GOVERNANCE, AUDIT,  
RISK MANAGEMENT  
AND STANDARDS  
COMMITTEE**

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|                             |   |
|-----------------------------|---|
| <b>Date of Meeting:</b>     | 25 January 2022   |
| <b>Subject:</b>             | <b>Information Report</b> – Invitation from Public Sector Audit Appointments to opt-in to external audits from 2023-24 to 2027-28 |
| <b>Responsible Officer:</b> | Dawn Calvert, Director of Finance and Assurance   |
| <b>Exempt:</b>              | No  |
| <b>Wards affected:</b>      | All   |
| <b>Enclosures:</b>          | None  |

## **Section 1 – Summary and Recommendations**

This report provides the committee with the opportunity to consider the invitation from the Public Sector Audit Appointments to opt-in to the appointment of external auditors for the period 2023-24 to 2027-28.

### **Recommendations:**

The Committee is asked to consider this report before full Council makes the formal decision.

## **Section 2 – Report**

### **Background**

1. The LB of Harrow along with the majority of Local Authorities uses Public Sector Audit Appointments (PSAA) for the procurement and appointment of external audit services.
2. The Council's current external auditors are Mazars LLP who were appointed to the LB of Harrow through the opt in sector led route of the PSAA.
3. Recent year's budgets have been set at the scale fees of £116,056 for the audit of the statement of accounts with separate additional fees for the Pension Fund and other grants and returns. Going forward scale fees will be put under pressure as changes are implemented to auditor's work on value for money arrangements and reporting.
4. The PSAA has invited all principal local government bodies to become opted-in authorities for the nomination of external auditors for the financial years 2023-24 to 2027-28.
5. The invitation is made in accordance with the Local Audit and Accountability Act 2014 and the Local Audit (Appointing Person) Regulations 2015 (the Regulations).
6. The length of the compulsory appointing period is for the five consecutive financial years commencing 1<sup>st</sup> April 2023.
7. A decision to become an opted in authority must be made in accordance with the Regulations, that is by Members at a full Council meeting and be made by 11<sup>th</sup> March 2022.
8. By not taking up the invitation from PSAA this Authority would have to procure an individual or joint contract with other authorities for external audit services and then set up an auditor panel.

### **Options Available**

9. There are three broad options open to the Council under the Local Audit and Accountability Act 2014 (the Act) which are set out below, each considered with their benefits and risks:

## **Option 1: Make a stand-alone appointment**

10. An Auditor Panel will need to be set up if a stand-alone appointment is made by the Council. The members of the panel must be wholly or be a majority of independent members as defined by the Act. Independent members for this purpose are independent appointees, this excludes current and former elected Members (or officers) and their close families and friends. This means that elected Members will not have a majority input to assessing bids and choosing which firm of accountants to award a contract for the Council's external audit. A new independent auditor panel would need to be established by the Council, in addition to the GARMS Committee. The Panel would be responsible for selecting the auditor and recommending their appointment to Full Council.

### **Advantages / benefits**

11. Setting up an auditor panel allows the Council to take full advantage of the new local appointment regime and have local input to the decision.

### **Disadvantages / risks**

12. Recruitment and servicing of the Auditor Panel, running the bidding exercise and negotiating the contract has been estimated in the past by the Local Government Association to cost in excess of £15,000 plus on going expenses and allowances. The Council would not be able to take advantage of reduced fees that may be available through joint or national procurement contracts. The assessment of bids and decision on awarding contracts will be taken by independent appointees and not solely by elected Members.

## **Option 2: Set up a Joint Auditor Panel / local joint procurement arrangements**

13. The Act enables the Council to join with other authorities to establish a joint auditor panel. Again this will need to be constituted of wholly or a majority of independent appointees (non-elected Members). Further legal advice would be required on the exact constitution of such a panel having regard to the obligations of each Council under the Act and the Council would need to liaise with other local authorities to assess the appetite for such an arrangement.

### **Advantages / benefits**

14. The costs of setting up the panel, running the bidding exercise and negotiating the contract will be shared across a number of authorities. There is greater opportunity for negotiating some economies of scale by being able to offer a larger combined contract value to the firms.

### **Disadvantages / risks**

15. The decision making body will be further removed from local input, with potentially no input from elected Members where a wholly independent auditor panel is used or possible only one elected Member representing each Council, depending on the constitution agreed with the other bodies

involved. The choice of auditor could be complicated where individual Councils have independence issues. An independence issue occurs where the auditor has recently or is currently carrying out work such as consultancy or advisory work for the Council. Where this occurs some auditors may be prevented from being appointed by the terms of their professional standards.

16. There is a risk that if the joint auditor panel choose a firm that is conflicted for this Council then the Council may still need to make a separate appointment with all the attendant costs and loss of economies possible through joint procurement.

### **Option 3: Opt-in to a sector led body (using Public Sector Audit Appointments (PSAA))**

17. To follow a sector led approach by which an 'appointing person' operates a nationwide, EU compliant procurement and appoints on the Council's behalf, maximising the opportunities for the most economic and efficient approach to procurement of external audit services on behalf of the whole sector. The PSAA continues to be the appointing person.

#### **Advantages / benefits**

18. The costs of setting up the appointment arrangements and negotiating fees would be shared across all opt-in authorities. By offering large contract values the firms would be able to offer better rates and lower fees than are likely to result from local negotiation. Any conflicts at individual authorities would be managed by the sector led body who would have a number of contracted firms to call upon.
19. Opting into the appointing person scheme removes the need to set up a separate independent auditor panel, comprising a majority of independent (non-elected) Members.
20. The PSAA has a specialist experienced team with technical expertise and extensive public sector knowledge when making auditor appointments. This provides the advantage of meeting all relevant regulations to appoint auditors, managing contracts with audit firms and setting and determining audit fees.
21. This option provides a transparent and independent external auditor appointment via a third party

#### **Disadvantages / risks**

22. Individual elected Members will have less opportunity for direct involvement in the appointment process other than through the Local Government Association and / or stakeholder representative groups. In order for the sector led body to be viable and to be placed in the strongest possible negotiating position the sector led body will need Councils to opt-in before final contract prices are known.

## Preferred option

23. Officers recommend the third Option, the sector led approach (using Public Sector Audit Appointments), as the most appropriate option for the Council to follow for the reasons set out above.

## Legal Implications

The appointment of the external auditor is required under the provisions of the Local Audit and Accountability Act 2014 and the requirements of the Local Audit (Appointing Person) Regulations 2015.

## Financial Implications

The Council does not make any direct payments to the PSAA for joining the national scheme. Other references to financial implications are contained within the main body of the report.

## Risk Management Implications

Risks included on corporate or directorate risk register? **No**

Separate risk register in place? **No**

The relevant risks contained in the register are attached / summarised below.

The following key risks should be taken onto account when agreeing the recommendations in this report:

| Risk Description  | Mitigations  | RAG Status |
|---|--|------------|
| Increased costs / lack of value for money caused by opting to appoint our own auditors (cost of administration of process plus potential higher external audit fees). | <ul style="list-style-type: none"><li>By opting into the PSAA scheme</li><li>The opt-in provides a value for money offer based on minimising PSAA costs and the distribution of any surpluses back to scheme members</li></ul> | Green      |
| Unable to secure the appointment of a qualified registered auditor.   | <ul style="list-style-type: none"><li>By opting into the PSAA scheme</li></ul>   | Green      |
| Lack of transparent / compliant procurement process   | <ul style="list-style-type: none"><li>By opting into the PSAA scheme and using their specialist team</li></ul>   | Green      |

## **Equalities implications / Public Sector Equality Duty**

Considering the Council's Public Sector Equality Duties under the Equality Act 2010, s.149, is integral to the decision- making process.

Was an Equality Impact Assessment carried out? No

There are no direct equalities implications.

## **Council Priorities**

The procurement process for appointing external auditors provides assurance that the Council has managed and delivered its finances in accordance with its approved plans and budget.

## **Section 3 - Statutory Officer Clearance**

### **Statutory Officer:**

Signed by the Chief Financial Officer

Dawn Calvert

**Date:** 12<sup>th</sup> January 2022

### **Statutory Officer:**

Signed on behalf of the Monitoring Officer

Blessing Enejo

**Date:** 12<sup>th</sup> January 2022

### **Chief Officer:**

Signed by Head of Procurement

Nimesh Mehta

**Date:** 12<sup>th</sup> January 2022

**Chief Officer:**

Signed for the Corporate Director

Dawn Calvert

**Date:** 13<sup>th</sup> January 2022

**Mandatory Checks**

Ward Councillors notified: NO, as it impacts on all Wards

**Section 4 - Contact Details and Background Papers**

**Contact:** Paul Gower (Interim Technical Accounting Manager)  
Tel: 020-8424-1335 Email: paul.gower@harrow.gov.uk

**Background Papers:**

None

If appropriate, does the report include the following considerations?

- |                |    |
|----------------|----|
| 1 Consultation | No |
| 2 Priorities   | No |

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