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COUNCIL MEETING

Wednesday, 30th July, 2014

7.30 pm

Town Hall, Watford

Publication date: 29 July 2014

CONTACT
If you require further information or you would like a copy of this agenda in another format, e.g. large print, please contact Caroline Harris on 01923 278372 or by email – legalanddemocratic@watford.gov.uk .

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Town Hall
Watford

29July 2014

Councillor

You are hereby summoned to attend a meeting of the Council of the Borough of Watford to be held on Wednesday, 30th July, 2014 starting at 7.30 pm at the Town Hall, Watford to take into consideration and determine upon the following subjects, namely: -

13. ICT ROADMAP (Pages 1 - 14)

Report of Director of Finance and ICT Client Section Head

14. MUNICIPAL BONDS (Pages 15 - 32)

Report of the Director of Finance

Manny Lewis, Managing Director

REPORT TO COUNCIL – 30th July 2014

REPORT OF CABINET – 23rd July 2014

Cabinet met on 23rd July 2014 The minutes have been circulated separately.

The following Members were present at the meeting:

Present:

Mayor Dorothy Thornhill	(Strategic partnerships/ external relationships and community safety)
Cllr D Scudder	(Deputy Mayor and Portfolio Holder for Corporate Strategy & Client Services.
Cllr Crout	(Community & Customer Services Portfolio Holder)
Cllr Johnson	(Portfolio Holder for Housing)
Cllr Sharpe	(Regeneration & Development Portfolio Holder)

Also present:

Councillors Nigel Bell (Labour)
Mo Mills (Labour)
Jackie Connal (Labour)
Peter Taylor (Liberal Democrat)

There was one recommendation to Council:

ICT ROADMAP

A report from the ICT Client Head and Director of Finance stated that additional Capital funds are required in order to meet the ICT improvements required. The report proposed to initiate a programme of ICT improvements. A detailed version of the roadmap proposal was approved at Joint Leadership team on 3 February 2014.

The Councils outsourced the ICT Service to Capita SIS in May 2013. Since outsourcing a number of problems raised during due diligence had been addressed either through specific and chargeable projects using existing budgets or through the managed service contract.

Despite some areas of improvement over the past few months there was still a recognition that the issues identified within due diligence posed a risk to the Council and that users were experiencing impaired performance in a variety of ways.

Therefore, project areas had been defined as an overall programme of ICT technical improvements from Capita SIS.

The Director of Finance commented that the Council needed to put in investment in order to make improvements due to the aging IT estate. This had also been brought about by the government's requirements for new security arrangements.

Councillor Bell questioned whether further investment would be needed on top of what the report was requesting.

The Mayor responded that investment would continue to be needed to bring the service up to standard. The Director of Finance commented that the investment would have been needed whether the Council had outsourced the service or not.

RESOLVED –

That Cabinet agrees to the additional capital budget required to complete the ICT improvements outlined in this report and **recommends that Council approves the necessary increase to the capital programme.**

Appendices

Report to Cabinet
Appendix 1 – Additional Project Details.
Appendix 2 – Detailed project costs for WBC

*PART A

Report to:	Cabinet
Date of meeting:	23 July 2014
Report of:	Emma Tiernan / Joanne Wagstaffe
Title:	ICT Roadmap

1.0 SUMMARY

1.1 Additional Capital funds are required in order to meet the ICT improvements required. This document provides a proposal to initiate a programme of ICT improvements.

A detailed version of this roadmap proposal has been approved at Joint Leadership team, on the 3 Feb 2014

2.0 RECOMMENDATIONS

2.1 Cabinet agrees to the additional capital budget required to complete the ICT improvements outlined in this report and recommends that Council approves the necessary increase to the capital programme.

Contact Officer:
For further information on this report please contact: Emma Tiernan, ICT Client Section Head.
telephone extension: 727457 email: emma.tiernan@watford.gov.uk

Report approved by: Joanne Wagstaffe, Director of Finance

3.0 **DETAILED PROPOSAL**

3.1 In May 2011, following a request from the Joint Leadership board, the Councils procured services to conduct an independent review of the internal shared ICT service. Recommendations within the Actica Infrastructure review contained critical work required in order to stabilise network infrastructure at both WBC & TRDC.

3.2 It was agreed by the ICT Steering Group and Joint Leadership team to focus on some of the essential infrastructure improvements e.g. replacing aged, business-critical servers, until the future of the delivery of the shared ICT service had been decided. This work commenced in Sept 2011 and finished in May 2012. In parallel to the Infrastructure Improvement programme, the Councils investigated options to outsource the internal ICT service.

3.3 The Councils subsequently outsourced the ICT service to Capita SIS in May 2013.

As part of the transition to a managed service provider the following process occurred:

- 2 stages of Capita due diligence
- Pre-contract due diligence, conducted once the appointment of preferred bidder was awarded and was reported at the 3 December 2012 ITSG
- Transition due diligence, which was a more detailed look at the Councils' ICT estates and was reported to the s.151 Officers and Head of ICT during 2013 and prior to transition.

The Councils conducted their own due diligence process, with the support of the WBC procurement manager as well as the support of Actica Consulting, who independently reviewed the due diligence stage of the tender.

3.4 Due diligence at the pre-award contract stage found the following:

- No up to date asset register
- Ageing assets (server, desktop estate, as well as network equipment and their related software)
- Some Single Points of Failure (primarily network related)
- Anti-virus and patching of servers – not up to date
- GCSX (now PSN – Public Services Network) accreditation – not achieved 2012/13
- PCI (Payment Card Industry) compliance – no self assessment performed in 2012/13
- Domain Topology - the arrangement of the various elements of a computer network. This relates to outstanding works from the implementation of shared services e.g. old WBC and TRDC parts of the network are still in situ.
- Administration Model – Absence of a "design" and common method of creating users, profiles etc
- No licence management across either Council – this relates to the management of software licenses

3.5 Due diligence at the transition stage expanded on the issues raised at the pre-award stage, but found further problems:

- A large number of Information Security related issues e.g. absence of up to

date security policies, no standard encryption tools in place.

- Aged database platform estate – Database platforms are the bits of software that sit underneath the business applications themselves. (At a high level imagine layers – Windows 2003 server, with an Ingres Database Platform, with the Revs and Bens Academy Database & Application on top of that.) A more commonly known database platform is Microsoft SQL. The W3R estate has a number of database platforms in place, Ingres, SQL and Oracle.
- Aged Business Applications and inconsistent documentation
- Poor physical network design – this relates to how the networks across W3R and all the sites that hang off the network talk to each other and physically sit together.
- Backups – Are running, but without formal controls and sufficient monitoring.
- Network bandwidth – this relates to the size of the pipes that transmit the data across the sites – between WBC and TRDC

3.6 Since outsourcing the service to Capita SIS, a number of the due diligence problems have been addressed either through specific and chargeable projects using existing budgets, or through the managed service contract:

- PSN accreditation achieved late 2013. Due to the large scope of this project, this did not just mean the Councils achieved that accreditation, but other risks and issues were also addressed within it:
    - All IT health check actions were addressed e.g. servers patched, therefore addressing security weaknesses on the server estates, software removed, updated etc. This therefore addressed a number of outstanding audit recommendations and requirements.
    - Additional layers of security added with the use of firewalls
    - Further security added to the remote working solutions
    - Solutions procured for use of portable devices
    - Updated security policies
- As a result of having to force network design changes to meet PSN requirements, this also compounded other network inadequacies. The Internal ICT service did not complete shared services IT projects and this has resulted in a “messiness” across the network, old routing tables in place, resulting in an unstable and inconsistent user experience. We therefore initiated a further project to clean that up.
- Asset audit was conducted as part of the transition to Capita
- PCI compliance. Aspects of this compliance regime have been met.
- The link between WBC and TRDC was upgraded to an appropriate size pipe.

3.7 Despite some areas of improvement over the past few months, there is still a recognition that the issues identified within due diligence pose a risk to the Council and that users are experiencing impaired performance in a variety of ways.

Therefore the following project areas have been defined as an overall programme of ICT technical improvements from Capita SIS.

It should be noted that an independent Enterprise Architect (Senior Technical role),

was supplied by Capita to review the due diligence findings, and to assess and make recommendations as to an appropriate way forward. In addition to this, his findings also provided an indication of the approach to the programme given the dependencies across each project area.

3.8 The programme of work for ICT to achieve a stable foundation, spans 20014/15 and can be described at a high level as follows. Please note, some projects are WBC specific, but primarily they are shared technically and therefore the costs are split with TRDC – 60/40:

Phase 1 – Preparation: (shared):

- Development of a Business IT strategy
- Active Directory Restructuring – Outstanding works
- Software Library and CMDB
- Licence Management
- Preparatory work for PSN (included within this is preparatory work for desktop refresh)

Subsequent Phases (shared):
Compliance Projects:

- PSN – Accreditation for 2014
    - Public Use Machines – Area within the Customer Service Centre
    - Mobile User Management (e.g. mobile phones)
- PCI Compliance

Aged Estate (shared):

- Desktop refresh
- Active Directory Migration (This is the database that manages users and groups)
- Database Migration
- Aged Server Refresh

Aged Estate (TRDC only)

- Exchange Upgrade – from 2003 (email)

Stability and Performance (shared):

- Network recommendations
- Phases 2 and 3 of domain topology
- Packaging applications

Stability and Performance (WBC Only):

- Thin Client Refresh
- Exchange Upgrade – from 2007 (email)

See Appendix 1 for details on each project.

3.9 There are a number of complex dependencies and external factors driving a large portion of this roadmap. Therefore in terms of phases and timing, the achievement of PSN accreditation is dependent on:

- Aged Estate:

- Desktop refresh – Moving from Win XP and Office 2003 to Win 7 and Office 2010
- Active Directory Migration – From 2003 to 2008/2012
- Database Migration – Various requirements here
- Server Refresh – Server 2003 to Server 2008 or 2012

3.10 All aspects of 3.9 link directly to each other. As an example please consider the following:

- Business application vendors have product roadmaps that we are contractually obliged to adhere to, as well as wanting to make use of new functionality. Normally the vendor will support the product provided within 2 versions of the latest release
- Those vendors test their "newer" products against later versions of Microsoft operating systems – both desktop and server, which therefore pushes us to migrate to later versions of Microsoft products
- Microsoft also have a de-support roadmap. This means they stop writing security updates and patches, therefore making systems and our network vulnerable
- Hardware relates to all of this, server and desktop estates need to be specified to the right level in order to allow those applications etc. to run and perform to the required standard
- PSN underpins this the requirement of us to be a trusted partner on the PSN network and therefore requires us means moving the entire estate to "supported" versions of Microsoft products

3.11 There are numerous benefits thereby improving service to users on a day to day basis:

- Business applications at a supported level – vendors not supporting the Councils on a "best endeavours" basis
- Desktop performance
- Reduced application downtime for key corporate applications e.g. Outlook for TRDC
- Standard desktop build – resulting in quicker deployment of new PCs etc

3.12 In order to ensure that the IT estate does not experience these issues in the future there are specific outcomes and deliverable built into the projects and the overall programme:

- Business Strategy development will give the authority a view and direction of a future applications roadmap. Therefore considering where additional investment may be required, and more importantly where savings and efficiencies can be generated. In addition to this, the development of this strategy will help to provide direction for other business-related projects across both Councils, e.g. Channel shift, Website review, Uniform Strategy.
- Technical strategy, will be developed so that there is a specific and scheduled rolling replacement programme of change, factoring in external dependencies such as Microsoft de-support, PSN.

3.13 Timing is an issue already, specifically for achieving PSN compliance for 2014. Our compliance timeframe is by the end of November 2014.

Other related risks:

- Throughout the due diligence reports, Capita has stated that service level waivers may need to be applied if sufficient action has not been applied to remedy some of these issues. We would have to further negotiate this with Capita SIS if the Councils choose not to invest
- Users continue to experience a lower than expected performance and this relates to understanding “What are users’ expectations?” “What are the expectations corporately?” “How do we measure these and gain a baseline to progress from?”
- PSN – the overall scope for 2014 has not been issued by the PSN authority. Primarily the risk here is in relation to unmanaged end use devices and potential costs in this area.
- Licence Management. The current licence estate position is not known. The Councils could be over- or under-subscribed. This is a particular risk for the Microsoft estate and could result in an additional required spend. However it could also mean that we can reduce business application licence costs and make some savings.

3.14 The governance of this programme is as follows:

- The programme of work is broken down into “phases” of work.
- Capita SIS would supply a detailed proposal for each phase, including key deliverables and user related improvements where appropriate.
- The overall budget is set for the programme and the Client Manager, with approval through ITSG “calls off” from that budget as phases are completed and signed off. This enables the Client function to appropriately challenge the Capita costs, deliverables and outcomes.
- Payment milestones will be used throughout each phase of the programme, and will be linked to key outcomes of each phase. These will all be agreed by ITSG.

3.15 The following structure will govern the roadmap:

- Programme Board consisting of representatives from each Council and Capita, who are responsible for day to day programme delivery. This group reports upwards to ITSG.
- ITSG act as the Senior Responsible Owner. This means that ITSG are reported to regarding this project and more specifically have the following roles:
    - Sign off the Communications Plan for the programme
    - Approve individual phases of work, based on cost, quality outcomes and a business case
    - Review, approve and sign off each completed phase, giving validation and/or recommendations for improvement before the programme

continues to the next stage

  - Give recommendations and approval to risks raised on a case by case basis as reported.

- Written and/or verbal updates will be given as required to the scrutiny committee overseeing the shared ICT service, as per the lead authority model arrangements.
- Lead members of the ITSG will be responsible for reporting "out" to senior management teams at each authority.
- Joanne Wagstaffe, Shared Director of Finance performs the role of Programme Executive.

4.0 IMPLICATIONS

Implications are listed below.

4.1 Financial

4.1.1 The estimated additional capital funds required for WBC to contribute are:

- £906,917.
- These funds include hardware, software and technical expertise in order to delivery the programme outlined above.
- This fund a contribution to an additional project support role of £37,500 but excludes any contingency costs.
- The remainder of the programme is funded via the use of unspent capital funds from 13/14, existing capital funds from 14/15, as well as a 40% contribution to shared projects from Three Rivers District Council.
- Appendix 2 has a breakdown of detailed project costs

4.1.2 The Shared Director of Finance comments that the additional costs can be funded from the usable capital receipts reserve.

4.2 **Legal Issues** (Monitoring Officer)

4.2.1 The Head of Democracy and Governance comments that as this is a new commitment it will require the approval of Council. Failure to upgrade our systems could well lead to security breaches and risks the integrity of data held by the Council and could potentially lead to breaches of the Data Protection Act 1998. Failure to achieve PSN compliance would lead to non delivery of essential services such as Revenues and Benefits and non compliance with our Individual Electoral Registration obligations.

4.3 Equalities

4.3.1 NA

4.4 **Potential Risks**

Potential Risk	Likelihood	Impact	Overall score
Service failures will continue	4	3	12
Failure to comply with PSN regulation: (Will occur if Windows XP desktop remains, Office 2003 remains, Windows Server 2003 remains)	4	3	12
Information security vulnerability – no patching of aged Desktop and server estate, thereby increasing our risk to Internet and virus related threats. (Will occur if Windows XP desktop remains, Office 2003 remains, Windows Server 2003 remains)	4	3	12

4.5 **Staffing**

4.5.1 1 additional and temporary staff member has been recruited for the period of the programme – to June 2015. This fund has been included within the costs section. This post is the Programme Support Officer.

4.6 **Accommodation**

4.6.1 Accommodation has been agreed at both WBC and TRDC in order to create a build space for the desktop refresh, stock control area and model office. The model office will be created for users to complete testing for the desktop refresh piece.

4.7 **Community Safety**

4.7.1 NA

4.8 **Sustainability**

4.8.1 NA

Appendices

Appendix 1 – Additional Project Details.
Appendix 2 – Detailed project costs for WBC

Background Papers

The following background papers were used in the preparation of this report. If you wish to inspect or take copies of the background papers, please contact the officer named on the front page of the report.

- Actica Infrastructure Review Document – 2011.
- Infrastructure Improvement Programme – Phase 2 Project Completion Report – May 2012.
- Actica – Final Report – Due Diligence Review – Conclusions – Dec 2012.

File Reference

- None

Appendix 1 – Additional Support Project Information

Preparation:

- Development of a Business IT Strategy. The Councils do not have an IT strategy that is informed by business need. This would drive future technological improvements, and ensure that the infrastructure platforms are fit for purpose, appropriate and meet the business requirements.
- Active Directory Restructuring – this work has already commenced in a phased approach and relates to sorting out network related "messiness". Users are inconvenienced by this such as through general inconsistent experiences across business applications, but there are many more.
- Software library and Licence Management – The Councils have no current and detailed knowledge of our licence estate and this is a risk, in terms of compliance with licence terms.

Compliance:

- PSN (Public Services Network). This is an annual requirement, which looks for LAs to meet an industry standard for Information Security. Failure to gain this accreditation impacts the authorities, as Revs & Bens and Elections services are unable to directly access data from other public sector bodies such as the DWP. PSN is a large scope project area, and the security requirements require the Councils to ensure areas of the network, publically accessible and in use e.g. CSC, training rooms, are secured to the required PSN standard. In addition to this, a large area of work relates to unmanaged end user devices e.g. mobile phones and home PCs, and this additional project will consider a solution for mobile phone management, again to adhere to compliance and best practice
- PCI Compliance. This is an annual self-assessment requirement and relates to the authorities' requirement to make financial transactions with members of the public.

Aged Estate:

- This is a variety of projects relating to aged hardware e.g. servers, desktops and network equipment and out of support software e.g. Microsoft Operating systems, Office products etc
- Desktops vary in age, and the current issues experienced, other than performance, is the inability to source spare parts. This therefore adds to delays to the delivery of fixes for users

Stability and Performance:

- A number of network recommendations have been made, including addressing risks around single points of failure across our network estates. These works, at a high level would reduce the impact, if hardware failures are experienced. However the risk should be assessed by the Councils on a case by case basis, to ensure that the solution is appropriate.
- The network recommendation findings are supported by previous internal audit recommendations. As an example the poor physical network design, was picked up by audit and has resulted in a recommendation to separate the network out according to a best practice standard. The user impact of this is potential instability seen across a variety of areas. All equipment on the network is given a unique identifier and this ID is used when equipment talks to each other. There have been instances of duplicate IDs being issued, causing conflicts and performance impairment across the network.
- Packaging Applications, means that Capita SIS can deploy PCs and application installations in a fraction of the time this currently takes. In addition

to this, the application roadmap can be developed and allows the Councils to proactively manage and control the licensing of all the products on the W3R estate

Other:

- As part of shared services, an original requirement was the ability to share free and busy information (calendars) between WBC and TRDC staff. This has never been achieved and could be through the upgrade and sharing of the Councils' email platforms.

Project Area	Estimated Cost	Authority	Totals
Phase 1			
Business Strategy	£0.00	Shared	
Active Directory Restructuring	£11,390.00	Shared	
Software Library and CMDB	£0.00	Shared	
License Management	£3,960.00	Shared	
Subsequent Phases			
Technical Governance	£55,506.00	Shared	
Ongoing Asset Admin	£33,000.00	Shared	
Desktop Refresh	£599,131.70	Shared	
Active Directory Migration	£98,416.00	Shared	
Server Refresh	£174,000.00	Shared	
Mobile User Management	£45,200.00	Shared	
Kiosk Public Access Computers	£17,790.00	Shared	
Network	£84,300.00	Shared	
PSN 2014 submission	£88,480.00	Shared	
PCI DSS Requirements definition	£8,400.00	Shared	
Server Monitoring	£0.00	Shared	
Data Centre Migration	£0.00	Shared	
Backup and Restore	£0.00	Shared	
Database migration	£29,640.00	Shared	
Application Packaging	£158,957.00	Shared	
			£1,408,170.70
	WBC 60% cont		**£844,902.42**
WBC Only			
Additional licenses required - E.g. MS Office	79,500	WBC	
Exchange Upgrade - 2007	£71,360.00	WBC	
Thin Client Refresh	£88,155.00	WBC	
			£1,083,917.42

Note: These are costs shared between WBC and TRDC. WBC contribution is 60%.

Existing capital budgets available (inc re-phased from 13/14)	-177,000
	£906,917.42

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REPORT TO COUNCIL – 30th July 2014

REPORT OF CABINET – 23rd July 2014

Cabinet met on 23rd July 2014

The following Members were present at the meeting:

Present:

Mayor Dorothy Thornhill	(Strategic partnerships/ external relationships and community safety)
Cllr D Scudder	(Deputy Mayor and Portfolio Holder for Corporate Strategy & Client Services.
Cllr Crout	(Community & Customer Services Portfolio Holder)
Cllr Johnson	(Portfolio Holder for Housing)
Cllr Sharpe	(Regeneration & Development Portfolio Holder)

Also present:

Councillors Nigel Bell (Labour)
Mo Mills (Labour)
Jackie Connal (Labour)
Peter Taylor (Liberal Democrat)

There were two recommendations to Council:

MUNICIPAL BONDS AGENCY

Cabinet received a report from the Director of Finance, the Local Government Association (LGA) was developing a proposal to establish a Municipals Bonds Agency. The benefits of doing this would be that local authorities should have access to cheaper rates of borrowing than may otherwise be the case.

The LGA were looking for authorities who may wish to invest in the Agency. This was in response to the LGA's view that the Public Works Loans Board (PWLB), currently the source of the majority of local authority borrowing, rates had become very expensive and inflexible.

The Director of Finance explained that the LGA needed to accumulate £8-10m in securities to go to Market, in order to get good rates and bond issue. If agreed, Watford would be supporting the agency through an investment of £20,000. The Director went onto explain that there was a risk the Council could lose the investment, however, there was good experience elsewhere and the prospect of a good return.

In response to a question from Councillor Bell, the Director of Finance commented that Stevenage Borough Council were also participating in the scheme and Birmingham City Council were contributing £200,000. Those Councils who were not investing were waiting to see what happened first, they did not have any specific issues with the scheme. The LGA now had enough investment to go forward with the first piece of work.

RESOLVED –

that Cabinet **recommends to Council that it**

- agrees to support the Local Government Agency in developing a Municipal Bonds Agency
- agrees to invest £20,000 into the Agency subject to approval of the final terms and conditions.

Appendices
Report to Cabinet
Appendix 1 – Municipal Bonds Agency Q&A from the LGA
Appendix 2 – Revised Business Case Summary from the LGA
Appendix 3 – Review of the Municipal Bonds Agency – Revised Business Case Summary from Capita

*PART A

Report to: Cabinet

Date of meeting: 23 July 2014

Report of: Joanne Wagstaffe

Title: Municipal Bonds Agency

1.0 SUMMARY

1.1 The Local Government Association (LGA) is developing a proposal to establish a Municipal Bonds Agency (the Agency). The benefits of doing this will be that local authorities should have access to cheaper rates of borrowing than they may otherwise be the case.

1.2 The LGA are looking for authorities who may wish to investing in the Agency. This report sets out a proposal for Watford Borough Council in response to the LGA Agency business case.

2.0 RECOMMENDATIONS

2.1 Cabinet agrees to support the Local Government Association in developing a Municipal Bonds Agency.

2.2 Cabinet agrees to invest £20,000 into the Agency subject to approval of the final terms and conditions.

Contact Officer:
For further information on this report please contact: Joanne Wagstaffe, Director of Finance.
telephone extension: 727200 email: Joanne.wagstaffe@watford.gov.uk

Report approved by: Joanne Wagstaffe, Director of Finance

3.0 **DETAILED PROPOSAL**

3.1 The LGA has been developing a proposal to establish a Municipal Bonds Agency. This is in response to it's view that the Public Works Loan Board (PWLB) borrowing rates have become expensive and relatively inflexible as a source of funding for local authorities. A list of Q&A provided by the LGA on the Agency can be found at Appendix 1.

3.2 The PWLB is currently the source of the majority of local authority borrowing. The Agency is designed to offer councils access to a cheaper rate of borrowing than those currently available from the PWLB.

3.3 The agency would borrow in bulk from the bond market and lend in smaller amounts to authorities of all sizes. This should enable authorities to access more competitive rates than they would otherwise be able to. The Agency may also arrange for lending or borrowing directly from local authorities. In addition it may also source funding from other third parties, such as banks, pension funds or insurance companies.

3.4 The LGA is looking to local authorities for investment to set up the Agency, which in turn will help other local authorities with their financial situation if they are in a borrowing position, through being able to offer cheaper borrowing rates.

3.6 There are a number of risks attached to setting up the Agency. The risks to the Agency are contained in the Revised Business Case Summary (Appendix 2) and in summary are:

- inability to raise the operating capital;
- demand for borrowing;
- market pricing;
- PWLB rates;
- Attracting the right people.

3.7 There are also risks to the Council in that it may not recover its initial investment in the Agency. Full risks will be known once the full details of the Agency are released. A review of the Revised Business Case has been undertaken by the Council's Treasury Management Advisers and this can be seen at Appendix 3.

3.8 The Agency is currently considering a joint and several guarantee from the borrowers. The joint and several guarantee would enable any amount which is in default to be distributed amongst those providing the guarantee. The guarantee will be provided by the local authorities borrowing from the Agency.

3.9 A joint and several guarantee would enable the Agency to borrow from the capital markets at a lower rate than it could otherwise. It will also enable the shares to be listed on the London Stock Exchange. This may result in a saving in borrowing costs of £7.2M over the life of a 30 year £100M loan. There are clearly risks attached to a joint and several guarantee but these may be mitigated by:

- Security over borrowing and the High Court process

- Proportionality/right of recourse
- The risk capital
- Statutory and budgetary controls in Councils
- The prudential code and the Minimum Revenue Provision
- The statutory responsibilities of Finance Directors (section 151 officers).
- Government Reserve Powers

3.10 Risk capital will be the required to provide protection against borrower default. This will be raised from the borrowers through holding back 3-5%. This will provide risk capital of 3-5% of the total loans provided. In reality this will mean that borrowers will have to borrow more than they require in order to provide the required risk capital.

3.11 The structure of the Agency has not been finalised but is expected to be a private sector company which will be owned by local government. It will have a Board of Directors which will have appropriate finance and capital markets experience. The Board will also include three members elected by the shareholders. It will have shares which will be transferable and therefore can be sold to other local authorities or other eligible public bodies.

3.12 Once the Agency has become established and a profit is being generated then dividends will be paid to shareholders. This will allow investors to start recouping their investments. Initial investors are expected to have more favourable terms than those which join at a later date.

3.13 Guidance from the LGA suggests that smaller authorities may wish to consider investing 10,000 - £50,000 in the Agency. It is therefore proposed that Watford Borough Council supports the Agency with a £20,000 investment.

3.14 The LGA is asking interested parties to issue a letter of intent, in advance of formal committee agreement, so as to gauge interest in the Agency. They would like this letter to be received by 12:00 noon on the 17th July 2014.

4.0 IMPLICATIONS

Implications are listed below.

4.1 Financial

4.1.1 It is proposed that a financial investment of £20,000 is made into the Agency subject to approval of the final terms. The investment prospectus has not yet been issued, but the investment is likely to be in the form of ordinary shares. The investment is likely to be in two stages, with the second stage dependent on further review of the project. The initial phase or mobilisation phased is estimated to require £400,000 and this will therefore limit the potential loss that any investors will incur.

4.1.2 The Council does not currently anticipate having to move into a borrowing position, over the life of the Medium Term financial Strategy, however, if this changes then one of the anticipated benefits of the Agency is lower borrowing rates which would be beneficial to the Council in the long term.

4.1.3 It should be noted that this is a start-up proposal and there is a real risk that some or all the equity investment might be lost if the Agency fails to succeed.

4.1.4 The Shared Director of Finance comments that the investment can be funded from the Economic Impact Reserve.

4.2 **Legal Issues** (Monitoring Officer)

4.2.1 The Head of Democracy and Governance comments that the Council has a general power of competence under the Localism Act 2011 that provides sufficient vires to enable it to take part in a company such as this. The documentation from the LGA refers to having had counsels opinion on the proposal but this has not been shared . The LGA have already set up a limited company and should cabinet choose to invest then the council would become a shareholder. The risks have been set out in the report. It is also not clear what level of further investment would be sought from initial shareholders in stage 2.

4.3 **Equalities**

4.3.1 NA

4.4 **Potential Risks**
4.4.1 These are contained in the report.

4.5 **Staffing**
4.5.1 NA

4.6 **Accommodation**
4.6.1 NA

4.7 **Community Safety**
4.7.1 NA

4.8 **Sustainability**
4.8.1 NA

Appendices

Appendix 1 – Municipal Bonds Agency Q&A from the LGA
Appendix 2 – Revised Business Case Summary from the LGA
Appendix 3 – Review of the Municipal Bonds Agency – Revised Business Case Summary from Capita

Background Papers

Establishment of a Local Government Collective Agency for the issue of Local Authority Bonds. A report to the Executive Board of the LGA March 2014.
http://www.local.gov.uk/documents/10180/11531/MBA+Report+Final.pdf/037bbcf0-e7f5-4f06-946e-98e7e824ce49

Municipal Bonds Agency Q & A

What will the Agency be?

It will be an independent company owned by local government with the sole aim of reducing financing costs for councils through arranging lending at competitive interest rates. It is envisaged that the company will fund lending through any or all of the following:

- *Raising money on the capital markets through issuing bonds*
- *Arranging lending or borrowing directly from local authorities*
- *Sourcing funding from other third party sources, such as banks, pension funds or insurance companies.*

What is the purpose of the Agency?

It will offer councils a viable alternative source of capital funding at a lower cost than existing sources and introduce sector owned diversity into the local government lending market. It will allow local authorities greater control over their funding costs in the future, by being able to demonstrate the value of peer pressure and capital market disciplines

Who would own it?

It will be owned solely by the local authorities or their pension funds that invest in its establishment. They will become shareholders in the Agency and therefore have a say in the way it is run. In due course, we would expect to be able to accommodate all local authorities, who wish to become shareholders.

Who would run it?

The Agency expects to have a wide local authority shareholder base. It will be a limited company, with its own Board of Directors comprising local authority finance experts, financial services experts from risk management and debt capital markets backgrounds and representatives elected by shareholders, all of who will go through a rigorous selection process.

How will councils recoup their investments?

It is envisaged that once the Agency is generating sufficient profit, it would be able to start paying a dividend to investors, while delivering economic benefits to borrowers. Its aim, as reflected in its incorporation documents, will be to deliver an overall benefit to the local government sector as a whole, and any future dividend policy set by its board would be subject to that. Its shares will be transferrable and therefore a council could sell its shares to other local authorities or eligible public bodies.

Does it have Ministerial support?

The Government's view is that it is within the powers of local authorities to establish a municipal bond agency. Ministers have said, "It remains for the local authority sector to determine collectively whether a local authority bond agency could be delivered on

a sustainable and affordable footing. It is consistent with the localism agenda that the autonomous local government sector considers whether it is able to deliver and sustain alternative financing models."

What happens if the Public Works Loans Board changes its interest rates?

The effect of PWLB rate change on the Bonds Agency's business would depend on its amount and how permanent the change was. The business case assesses the risk from future PWLB competition. Nevertheless the Treasury has said publicly that reducing PWLB margins is not being considered.

How long will it take to establish the Agency?

The business case assumes that the Agency would be ready to issue its first bonds in March/April 2015 to meet the normal peaks in council demand for borrowing.

Is additional legislation required to enable the Agency to be established?

No. Councils have the necessary powers.

What impact will this proposal have on the Government's control of overall government borrowing?

Nothing in this proposal seeks to change existing arrangements. The proposals do not facilitate additional borrowing over what is already permitted within the capital regulatory system. The existing arrangements with the Government retaining ultimate regulatory control are to be maintained and borrowing authorities will be required to operate within the current prudential code. What it will do is, for any given level of borrowing, reduce the interest bill local taxpayers have to fund.

Is it legal for councils to guarantee each other's debts?

Our very clear legal advice is that the General Power of Competence (GPC) introduced in the Localism Act 2011 gives English councils the power to do this. Because the GPC does not cover other public bodies such as Police, Fire and National Park Authorities, it is less clear whether they could do the same without a change in the legislation, which applies to them.

Should councils be concerned about providing a joint and several guarantee?

The Agency will have in place a credit process, underpinned by ongoing monitoring; risk and liquidity capital; and a right of recourse, which will ensure, in the event of the guarantee being called, that it will be applied proportionally. Even were the guarantee to be called, creditors would be confident of receiving their money back in time. The protections available would be stronger than currently apply in the case of inter-council lending. Nevertheless, no local authority has ever defaulted and for the joint and several guarantee to be called an unprecedented situation would have arisen.

What controls are in place to prevent a default and what measures are available to a council to recover sums owing to it?

There are a range of controls designed to prevent a Local Authority from defaulting on its obligations. In addition, there are legislative measures that are likely to ensure that even if a Local Authority does default, its creditors are able to recover sums owing to them. These controls and measures include:

- *Councils are statutorily prevented from borrowing to avoid raising taxes and cutting spending, thereby reducing the risk of a council entering financial distress.*
- *The prudential code forces councils to consider whether borrowing is affordable and financially sustainable.*
- *The responsibility of Section 151 officers under Section 114 of the Local Government Finance Act 1988 to ensure that councils can meet their obligations as they fall due, and to formally report if the council's expenditure will exceed its resources.*
- *Continuing access to the PWLB for liquidity support.*
- *Government reserve powers to intervene. To date, the Government has not allowed any Local Authority to default on its obligations.*
- *If a Local Authority defaults on a debt greater than £10,000 for a period of two months, under Section 13(5) of the Local Government Act 2003 a creditor may apply to the High Court for an administrator to be appointed. This process should ensure that any Local Authority that is called upon under the guarantee can recover the debt via the courts if need be. The powers of the administrator will be determined by the High Court, but can include:*
    - *Collecting, receiving or recovering the revenues of the local authority*
    - *Issuing levies or precepts; or*
    - *Setting, collecting or recovering Council Tax.*

What is the reaction of local authorities to the establishment of an agency?

A significant number of local authorities have been very supportive of the initiative to date, devoting time and resources to help ensure that the business case is fully robust. As part of the business case review, we carried out a survey of English councils and, in addition, presented at a number of local authority conferences. Since publishing the revised business case we have spoken directly to over 90 councils. These recent conversations, the survey, and conference feedback, have confirmed to us that there is significant demand for an alternative, local authority controlled, source of capital finance

How much will it cost?

We are looking to raise £8 to £10 million capital, which includes a buffer to ensure that the agency is well capitalised. Our project plans envisage that this will be used within a staged process, with a number of checkpoints overseen by a rigorous governance process. We have established the Local Capital Finance Company Ltd and have now presented a firm investment proposition to all councils and related bodies, such as local authority pension funds, in an Information Memorandum.

Haven't local authorities stopped borrowing money and therefore will there be a sufficient volume to support the agency's business plan?

It is correct that volumes of local authority borrowing have reduced recently. There are a number of reasons for this: low interest rates have resulted in councils doing more short term borrowing from each other; many councils have a legacy of long dated debt overhang and LOBO structures; and councils have reduced capital spending, partly driven by reduced headroom on their revenue accounts and recent austerity measures. However, discussions with councils reveal significant future demand for borrowing, which will be required for: local enterprise partnerships, city deals, town centre rejuvenation projects, roads, housing, schools and simply to maintain the nation's capital stock. The maintenance backlog on local roads alone now stands at £12 billion.

Will the Agency require councils to undergo a credit process?

Yes. Providers of finance, be they bond market investors, banks or non-bank providers of credit will expect a credit process to have been undertaken. The credit process will underpin the agency's credit rating, thus enabling it to achieve the keenest rates of interest. The credit process will be tailored to councils and the Agency and will not be excessively onerous.

Will borrowers have to pay interest rates higher than PWLB interest rates?

We cannot foresee circumstances when this would occur. Section 8 (page 53) of the business case sets out the pricing strategy, which is driven by the need for the Agency to deliver savings to its local authority borrowers. It can be found at this link:

Local Government Association

Municipal Bonds Agency

Revised Business Case Summary

20 March 2014

Public interest case

1. Councils source 75 per cent of their borrowing from the Public Works Loans Board (PWLB). That leaves councils vulnerable to interest rates set to deliver the government's public borrowing plans. The Municipal Bonds Agency would give councils greater control of interest rates and introduce competition and diversity to the marketplace. The Agency could also offer lower penalties for early repayment of loans.

2. Nordic experience has shown that an agency's credit processes, with the incentive of lower borrowing costs and the oversight of peers, has strengthened the overall credit worthiness of local authorities.

3. The experience of the Nordic Agencies has also shown that the Agency could pass onto councils the benefit of its research into public sector financing. From this expertise it would be possible to develop advisory and tailored lending services and potentially facilitate intra authority lending.

Local Authority and investor demand

4. Councils will have new borrowing requirements for their capital programmes. Our survey identified a borrowing requirement of £5 billion over the next three years from just 46 councils, with 43 expressing an interest in using the Agency. The outstanding stock of PWLB debt matures at £1.7 billion a year. Much of that will require refinancing. Borrowing from banks is forecast to become increasingly expensive. It is estimated that annual local authority borrowing over the next three years will be between £3billion and £5 billion.

5. Banks have indicated a likely significant investor demand for the Agency's bonds. At the same price as Transport for London (TfL)'s double-A rated bonds, council borrowers would save around five basis points (bps) against the PWLB certainty rate (80bps). To achieve better bond pricing, the Agency would need an AAA/sovereign like rating. That could be achievable by holding risk capital between three and five per cent; holding adequate liquidity; providing a joint and several guarantee from borrowers; and ensuring a diverse portfolio of borrowers. An AAA/sovereign like rating combined with a joint and several guarantee should deliver significant savings to borrowers.

6. Because the Agency will be new to the market, it is likely to need to pay a new issue premium in the first one to two years. This will affect the level of savings available to early borrowers. The savings in the previous paragraph will also depend on being able to issue bonds in benchmark sizes of between £250 million to £300 million; otherwise investors will demand a premium for illiquidity.

Joint and several guarantee

7. A joint and several guarantee creates the prospect of much cheaper borrowing. It will also enable the bonds to be listed on the London Stock Exchange. Overall a joint and several guarantee could expect to reduce the Agency's borrowing costs by 20 to 25 bps, saving £6.2 million to £7.5 million over the life of a 30 year £100million loan. The risks of offering a joint and several guarantee are mitigated by:
8.
    - Security over borrowing and the High court process
    - Proportionality/right of recourse
    - The risk capital and liquidity of the Agency
    - The Agency's credit processes
    - Statutory and budgetary controls in councils

- The prudential code and minimum revenue provision
- The statutory responsibilities of Finance Directors (section 151 officers)
- Access to the PWLB
- Government reserve powers.

Operating model and capital structure

9. The Agency should issue two bonds in its first year with approximately 30 to 40 borrowers. For the initial issues, council borrowing will need to match the bonds' maturity profiles. Agency staffing will start small and grow as the volume of transactions does. Most functions will be outsourced. The Agency is expected to break even by year three after around £2 billion of bond issuance. It is estimated £8 million to £10 million of operating capital will be needed to cover launch and early operating costs and provide a buffer against risks.

10. The Agency's operating capital should be raised from councils or related bodies as common equity. An equity structure would allow the trading of shares and give the Agency a decision making framework over profit retention and dividends. The shareholding structure would have limits on individual level of control and give a fair return to initial shareholders for risk taking. Voting and economic rights should be de-coupled.

11. Risk Capital will be required to support the first loss protection in the event of a borrower default and should be equivalent to three to five per cent of the loans made to councils. It will be raised through a proportion of a loan taken out by a borrower being retained by the Agency.

Timeline

12. The Agency should aim to issue its first bond to match the March/April 2015 peak in council borrowing. A mobilisation phase should start once the decision to proceed is made and last six months. The mobilisation phase will cost approximately £0.8 million and would establish the corporate structure; hire of key personnel; establish the Board; identify the initial list of borrowers and investors in the Agency; design key policies and processes.

Governance

13. Control should rest with the LGA as the project sponsors in mobilisation phase. A project board should oversee execution, with CFO and political groups retaining an advisory role. Once appointed the Board of Directors (BoD) may operate in a shadow capacity until launch. The project board in consultation with the BoD will determine the point at which the project moves into launch.

14. At launch, the BoD will formally take control of the Agency. The BoD will consist of: three members elected by shareholders, one of whom will be the Chair; a debt capital markets expert; a risk management expert; two council finance directors or equivalent. The CEO may be a Director. The initial board will be appointed by the LGA in conjunction with the project board and in consultation with the shareholders.

Risk

15. There are five key risks at this stage the most significant being that it may not be possible to raise the operating capital from councils or related bodies, despite it being an attractive investment. Other risks relate to council demand; market pricing; PWLB lowering its interest rates; and attracting the right calibre of personnel.

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CAPITA

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Review of Municipal Bonds Agency – Revised Business Case Summary

11 April 2014

Review of Municipal Bonds Agency – Revised Business Case Summary

1. Background

In recent days, many clients will have been contacted by the Municipal Bonds Agency with a view to determining whether their authority may wish to express an interest in participating in a new cash lending facility. This facility will compete directly with other sources of funding, including that offered by the Public Works Loan Board. Expressions of interest have been sought in respect of either borrowing from this facility at a later date, or providing initial capital for the venture.

Capita Asset Services welcomes this potential new lending facility, but we are also aware that there are several additional areas which need to be addressed as part a comprehensive due diligence process before we can provide a definitive view.

2. Revised Business Case Summary

On 20th March, the Municipal Bonds Agency circulated a Revised Business Case Summary. We have reviewed the content of this document and have the following comments to make which we hope are both helpful to potential participants and the Bonds Agency itself.

Public interest case

Para 1 – Although the Municipal Bonds Agency would be potentially injecting new competition into the loans market, interest rates are set by the market participants (including banks, fund managers, pension fund managers etc) and the Agency may, therefore, have less control or influence over offered rates than it anticipates.

Local Authority and investor demand

Para 4 – There is an assumption that significant refinancing of existing loans portfolios will occur over the next three years, but depending on the speed of the recovery of the UK economy, there may actually be a propensity for authorities to further internally borrow if both resources permit and the cost of carry remains high (the differential between borrowing and investment rates). This of itself is a risk to the Agency's proposed business plan. In addition, as discussed at the recent round of Capita Asset Services seminars, there are a reasonable amount of authorities with a declining Capital Financing Requirement profile, which argues against any long-term funding being taken on board in the near-term.

Para 5 – An initial saving of 0.05% in interest payments is referred to, compared to the PWLB Certainty Rate, but this assumption is based on the success of the AA rated Transport for London issue. This organisation is one of the largest and best known participants in the public sector bond market. The Agency states that it will seek to gain a AAA rating but one of the criterion proposed by the Agency for moving towards this objective is the holding of 3%-5% risk capital. The question is, who is going to provide that capital and what interest would they anticipate receiving for their support and how are those costs to be recovered? It may also be difficult to get a AAA rating as the UK Government has been cut to AA+. It has been suggested that the capital will come from the lenders: for example, for £100m a council would borrow £105m, leaving £5m with the Agency. However, this would appear to have the

effect of pushing the loan rate up as, for instance, a 4% coupon would in reality be 4.20% with this additional funding approach.

Para 6 – There is a reference to a "new issue premium" in the first year or two. Which "early joiner" authorities would voluntarily pay a higher interest rate on new borrowing than is offered by the PWLB. Could this lead to value-for-money audit issues?

Joint and several guarantee

Para 7 – There is reference to a "joint and several guarantee". We would be interested to know whether there is Counsel's opinion supporting this proposal from a legal standpoint and also whether the market view of this proposal would really support the supposition that another 0.25% reduction in interest rates would follow.

Para 8 – There is a reference to the Agency's credit processes adding weight to the joint and several liability guarantee. What are the processes that are referred to?

Operating model and capital structure

Para 9 – The crucial point here is how flexible can the Agency be in respect of the bond maturity profiles and how will it ensure that its bonds are what its potential customers want in respect of size, duration and interest rate given the volatility of the markets intra-year? Will 30 or 40 borrowers all want the same monies for the same periods?

Para 10 – There is a lack of detail as to how the statement "the shareholding structure would have limits on individual level of control and give a fair return to initial shareholders for risk taking" would operate in practice.

Para 11 – The proposal for a proportion of any loan being taken out by an authority being retained by the Agency suggests close scrutiny needs to be paid to the net interest savings calculations quoted by the Agency.

Timeline

Para 12 – The assertion that authorities base their borrowing on a March/April peak, and that any bond issue would reflect this profile, is somewhat outdated given authorities now have to contend with a low interest rate environment where the "normal" Bank Rate may not. be much greater than 3% in the coming years. This backdrop could potentially undermine the attractiveness of longer dated bond durations.

Risk

Para 15 – Is it an attractive investment? In CAS's view, now is not the right time in the interest rate cycle to be lending long-term. This is based on various interest rate forecasts that long-term rates will increase over the medium to longer term. Also, following on from para 5, rates could and often do move by more than 0.05% in any one day, so the "savings" differential could be wiped out quite quickly, even before the overall costs of the bond are taken into consideration.

In addition, will the UK Government be happy that a competitor to the PWLB has emerged – one only has to look at the HRA self-financing reform process as an example of how the Treasury has the immediate ability to price PWLB loans to be lower than those offered by the

market. A comparison to the Nordic approach, whilst interesting, does not help in clarifying the UK Government's competitive intentions in this respect.

We hope that you find the above a useful starting point for your own internal review processes, and please feel free to speak to your Client Relationship Manager if you wish to discuss any of the aforementioned points in more detail. We do believe that it is a good development, however there are a number of issues which need to be resolved.

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