# Isle of Wight Council

# TREASURY MANAGEMENT STRATEGY

## 2015-16

## Updated September 2015

# Document Information

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| 3.0 | 14 September 2015 | Revision for Waste contract borrowing and additional capital from Exec 15/9 |

# Contents

# 1. Introduction

In February 2003 the Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year.

In addition, the Department for Communities and Local Government (CLG) issued revised *Guidance on Local Authority Investments* in March 2010 that requires the Council to approve an investment strategy before the start of each financial year.

This report fulfils the Council's legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the CLG Guidance.

The Council has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the Council's treasury management strategy.

# 2. External Context

**Economic background:** UK economic growth picked up as expected in Q2 following softer activity in Q1; the second estimate confirmed Q2 GDP growth was 0.7%. This followed 2014 full year growth of 3.0%. Annual GDP growth is projected to fall back from rates seen in 2014 and settle a little above 2½%.

Inflation is currently very low and, with the further fall in commodity prices, will remain so in the near-term. The CPI rate is likely to rise towards the end of 2015 due to base line effects. The MPC is likely to look through temporary periods of very low inflation, as it has done when inflation has been well above the 2% target.

At its meeting ending on 9 September 2015, the Monetary Policy Committee (MPC) voted by a majority of 8-1 to maintain Bank Rate at 0.5%.

**Credit outlook:** The transposition of two European Union directives into UK legislation in the coming months will place the burden of rescuing failing EU banks disproportionately onto unsecured local authority investors. The *Bank Recovery and Resolution Directive* promotes the interests of individual and small businesses covered by the Financial Services Compensation Scheme and similar European schemes, while the recast *Deposit Guarantee Schemes Directive* includes large companies into these schemes. The combined effect of these two changes is to leave public authorities and financial organisations (including pension funds) as the only senior creditors likely to incur losses in a failing bank after July 2015.

The continued global economic recovery has led to a general improvement in credit conditions since last year. This is evidenced by a fall in the credit default swap spreads of banks and companies around the world. However, due to the above legislative changes, **the credit risk associated with making unsecured bank deposits will increase** relative to the risk of other investment options available to the Council.

**Interest rate forecast**: The Council's treasury management advisor Arlingclose forecasts the first rise in official interest rates in June 2016, and a gradual pace of increases thereafter, with the average for 2015/16 remaining at 0.5%. Arlingclose believes the normalised level of the Bank Rate post-crisis to range between 2.0% and 3.0%.
For the purpose of setting the budget, it has been assumed that new investments will be made at an average rate of 0.25%, and that no new long-term loans will be taken; all borrowing will be for periods of less than 364 days at an average rate of 1.14%. These assumptions for the main part remain unchanged in this update.

## 3. Local Context

As at 31 August 2015, the Council has £119.4 million of external borrowing and £4.5 million of investments. This is set out in further detail at ***Appendix B***. Forecast changes in these sums are shown in the balance sheet analysis in table 1 below.

Table 1: Balance Sheet Summary and Forecast

| | **31.3.14 Actual £m** | **31.3.15 Actual £m** | **31.3.16 Estimate £m** | **31.3.17 Estimate £m** | **31.3.18 Estimate £m** |
|---|---|---|---|---|---|
| **General Fund CFR** | **225.2** | **246.5** | **280.2** | **315.6** | **357.3** |
| Less: Other debt liabilities * | (28.9) | (50.9) | (68.2) | (84.9) | (101.6) |
| **Borrowing CFR** | **196.3** | **195.6** | **212.0** | **230.7** | **255.7** |
| Less: External borrowing ** | (154.4) | (133.7) | (122.9) | (107.9) | (99.9) |
| **Internal borrowing** | **41.9** | **61.9** | **89.1** | **122.8** | **155.8** |
| Less: Usable reserves | (46.9) | (52.9) | (52.8) | (57.1) | (60.1) |
| Less: Working capital surplus | (0.4) | (12.7) | (12.7) | (12.7) | (12.7) |
| **Investments (or New borrowing)** | **5.4** | **3.7** | **(23.6)** | **(53.0)** | **(83.0)** |

* finance leases and PFI liabilities that form part of the Council's debt
** shows only loans to which the Council is committed at 10 September 2015 and excludes optional refinancing

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

The council's total CFR is increasing due to the contracted capital expenditure arising under the highways PFI contract. This is funded through the unitary charge, and is spreads over the 25 year contract.

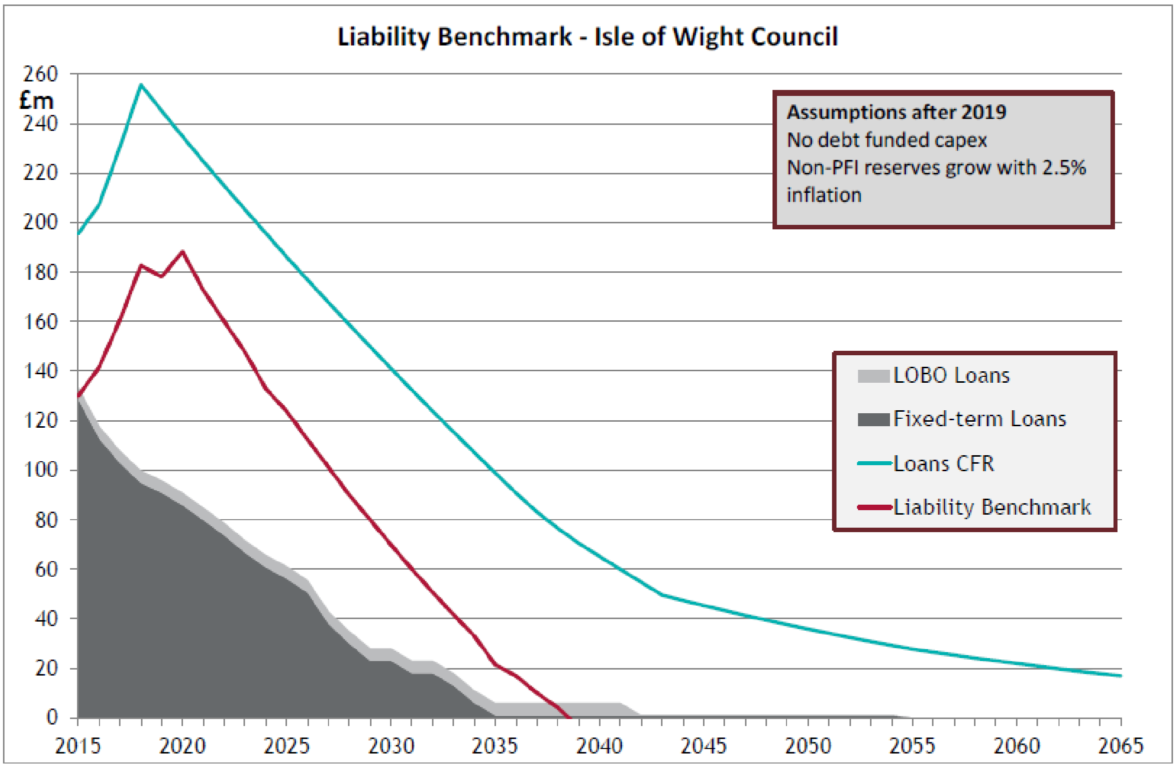
The council's borrowing CFR is increasing as a result of the new Waste project which was approved by the council in July 2015, including the need to borrow approximately £80 million over the life of the contract, £70 million of which is required in the first three years.

CIPFA's *Prudential Code for Capital Finance in Local Authorities* recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 shows that the Council expects to comply with this recommendation during 2015/16.

To assist with its long-term treasury management strategy, the Council and its advisers have created a liability benchmark, which forecasts the Council's need to borrow over a 50 year period. Following on from the medium term forecasts in table 1 above, the benchmark assumes:

- No capital expenditure, other than in respect of the waste contract, funded by borrowing
- minimum revenue provision on new capital expenditure based on a 52 year asset life
- PFI cash flows according to the project plan
- income, expenditure and reserves all increase by 2.5% inflation a year

## Liability Benchmark



The shaded area of the chart above reflects the maturity profile of the council current external borrowing. The red line indicates the net borrowing requirement as calculated from table 1 above and extended beyond the forecast period. The blue line is the council's underlying borrowing requirement, based on historic capital expenditure.

The gap between the red and blue lines indicates the amount of internal resources used to fund the council's capital programme – being reserves. In the period to 2018 this gap increases due to the accumulation of PFI reserves to fund the capital lump sum payments in 2017-18 through 2019-20. In 2020 the gap is at its narrowest, reflecting the full utilisation of that reserve.

The gap between the shaded area and the red line demonstrates the net borrowing requirement for the council, at around £83 million by 2018.

# 4. Borrowing Strategy

At 31 August 2015, the Council held £119.4 million of loans, a decrease of £24.5 million on the previous year end, as part of its strategy for funding previous years' capital programmes. The balance sheet forecast in table 1 shows that the Council expects to borrow up to £23.6 million in 2015-16, primarily to cover the capital requirements of the waste contract, but including up to £6 million of new borrowing to fund capital expenditure. The Council may also borrow additional sums to pre-fund future years' requirements, providing this does not exceed the authorised limit for borrowing of £212.0 million.

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

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

By doing so, the Council is able to reduce net borrowing costs (despite foregone investment income) and reduce overall treasury risk. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. Arlingclose will assist the Council with this 'cost of carry' and breakeven analysis. Its output may determine whether the Council borrows additional sums at long-term fixed rates in 2015/16 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

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

It is proposed that for the first three years of the waste contract (starting November 2015) all borrowing to finance the capital investment will be sourced from short term (less than 364 days borrowing, to take account of currently forecast ongoing low interest rates. It is proposed that at specified future dates, parcels of this short term debt will be refinanced via fixed rate, long term debt, to mature at the end of the contract (financial year 2040-41), repayable by equal instalments of principal for the period of the loans.

**Sources:** The approved sources of long-term and short-term borrowing are:

- Public Works Loan Board (PWLB) and its successor body
- any institution approved for investments (see below)
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except Isle of Wight Council Pension Fund)
- capital market bond investors
- Local Capital Finance Company and other special purpose companies created to enable
- local authority bond issues

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

- operating and finance leases
- hire purchase
- Private Finance Initiative
- sale and leaseback

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

**LGA Bond Agency:** Local Capital Finance Company was established in 2014 by the Local Government Association as an alternative to the PWLB. It plans to issue bonds on the capital markets and lend the proceeds to local authorities. This will be a more complicated source of finance than the PWLB for three reasons: borrowing authorities may be required to provide bond investors with a joint and several guarantee over the very small risk that other local authority borrowers default on their loans; there will be a lead time of several months between committing to borrow and knowing the interest rate payable; and up to 5% of the loan proceeds will be withheld from the Council and used to bolster the Agency's capital strength instead. Any decision to borrow from the Agency will therefore be the subject of a separate report to Audit Committee.

**LOBOs:** The Council holds £5.0 million of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate as set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. The total amount of these LOBOs have options during 2015/16, and although the Council understands that lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Council will take the option to repay LOBO loans at no cost if it has the opportunity to do so. Total borrowing via LOBO loans will be limited to £15m.

**Short-term and Variable Rate loans**: These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

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

# 5. Investment Strategy

The Council holds invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Council's investment balance has ranged between £2.1 and £33.7 million, due to short-term (364 day) borrowing taken at the end of last financial year, for longer periods than eventually required. For 2015-16, surplus balances will range between £0 and £9.0 million, as borrowing durations will be restricted to cover periods of need only, not automatically set at 364 days.

Additional investments will be undertaken in respect of the capital receipt for the sale of land to Asda, up to a maximum of £20 million. These investments will be managed separately from the council's operating surpluses.

**Objectives:** Both the CIPFA Code and the CLG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk receiving unsuitably low investment income.

**Strategy:** Given the increasing risk and continued low returns from short-term unsecured bank investments, the Council aims to further diversify into more secure and/or higher yielding asset classes during 2015/16. This is especially the case for the potential £20 million that may be available for longer-term investment, subject to anticipated capital receipts. All of the Council's surplus cash is currently invested in short-term unsecured bank deposits and money market funds. This diversification will therefore represent a substantial change in strategy over the coming year.

**Approved Counterparties:** The Council may invest its surplus funds with any of the counterparty types in table 2 below, subject to the cash limits (per counterparty) and the time limits shown.

Table 2: Approved Investment Counterparties and Limits

| Credit Rating | Banks Unsecured | Banks Secured | Government | Corporates | Registered Providers |
|---|---|---|---|---|---|
| UK Govt | n/a | n/a | £ Unlimited 50 years | n/a | n/a |
| AAA | £4.0m 5 years | £4.0m 20 years | £4.0m 50 years | £4.0m 20 years | £4.0m 20 years |
| AA+ | £4.0m 5 years | £4.0m 10 years | £4.0m 25 years | £4.0m 10 years | £4.0m 10 years |
| AA | £4.0m 4 years | £4.0m 5 years | £4.0m 15 years | £4.0m 5 years | £4.0m 10 years |
| AA- | £4.0m 3 years | £4.0m 4 years | £4.0m 10 years | £4.0m 4 years | £4.0m 10 years |
| A+ | £4.0m 2 years | £4.0m 3 years | £4.0m 5 years | £4.0m 3 years | £4.0m 5 years |
| A | £4.0m 13 months | £4.0m 2 years | £4.0m 5 years | £4.0m 2 years | £4.0m 5 years |
| A- | £4.0m 6 months | £4.0m 13 months | £4.0m 5 years | £4.0m 13 months | £4.0m 5 years |
| BBB+ | £2.0m 100 days | £4.0m 6 months | £2.0m 2 years | £2.0m 6 months | £2.0m 2 years |
| BBB or BBB- | £2.0m next day only | £4.0m 100 days | n/a | n/a | n/a |
| None | £1.0m 6 months | n/a | £4.0m 25 years | £50,000 5 years | £4.0m 5 years |
| Pooled funds | £4.0m per fund | | | | |

This table must be read in conjunction with the notes below

**Credit Rating:** Investment decisions are made by reference to the lowest published long-term credit rating from Fitch, Moody's or Standard & Poor's. Where available, the credit rating relevant to the specific investment or class of investment is used, otherwise the counterparty credit rating is used.

**Banks Unsecured:** Accounts, deposits, certificates of deposit and senior unsecured bonds with banks and building societies, other than multilateral development banks. These investments are subject to the risk of credit loss via a bail-in should the regulator determine that the bank is failing or likely to fail. Unsecured investment with banks rated BBB or BBB- are restricted to overnight deposits at the Council's current account bank, National Westminster Bank/Royal Bank of Scotland.

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

**Government:** Loans, bonds and bills issued or guaranteed by national governments, regional and local authorities and multilateral development banks. These investments are not subject to bail-in, and there is an insignificant risk of insolvency. Investments with the UK Central Government may be made in unlimited amounts for up to 50 years.

**Corporates:** Loans, bonds and commercial paper issued by companies other than banks and registered providers. These investments are not subject to bail-in, but are exposed to the risk of the company going insolvent. Loans to unrated companies will only be made as part of a diversified pool in order to spread the risk widely.

**Registered Providers:** Loans and bonds issued by, guaranteed by or secured on the assets of Registered Providers of Social Housing, formerly known as Housing Associations. These bodies are tightly regulated by the Homes and Communities Agency and, as providers of public services, they retain a high likelihood of receiving government support if needed.

**Pooled Funds:** Shares in diversified investment vehicles consisting of the any of the above investment types, plus equity shares and property. These funds have the advantage of providing wide diversification of investment risks, coupled with the services of a professional fund manager in return for a fee. Money Market Funds that offer same-day liquidity and aim for a constant net asset value will be used as an alternative to instant access bank accounts, while pooled funds whose value changes with market prices and/or have a notice period will be used for longer investment periods.

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

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

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

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

**Other Information on the Security of Investments**: The Council understands that credit ratings are good, but not perfect, predictors of investment default. Full regard will therefore be given to other available information on the credit quality of the organisations in which it invests, including credit default swap prices, financial statements, information on potential government support and reports in the quality financial press. No investments will be made with an organisation if there are substantive doubts about its credit quality, even though it may meet the credit rating criteria.

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

**Specified Investments**: The CLG Guidance defines specified investments as those:

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and
- invested with one of:
  - the UK Government,
  - a UK local authority, parish council or community council, or
  - a body or investment scheme of “high credit quality”.

The Council defines “high credit quality” organisations and securities as those having a credit rating of A- or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of A- or higher.

**Non-specified Investments**: Any investment not meeting the definition of a specified investment is classed as non-specified. The Council does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition on high credit quality. Limits on non-specified investments are shown in table 3 below.

Table 3: Non-Specified Investment Limits

| | **Cash limit** |
|---|---|
| Total long-term investments | £30m |
| Total investments without credit ratings or rated below A- | £5m |
| Total investments with institutions domiciled in foreign countries rated below AA+ | £5m |
| Total non-specified investments | £40m |

**Investment Limits**: The Council's revenue reserves available to cover investment losses are forecast to be £32 million on 31st March 2015. In order that no more than 15% of available reserves will be put at risk in the case of a single default, the maximum that will be lent to any one organisation (other than the UK Government) will be £4.0 million. A group of banks under the same ownership will be treated as a single organisation for limit purposes. Limits will also be placed on fund managers, investments in brokers' nominee accounts, foreign countries and industry sectors as below:

Table 4: Investment Limits

| | **Cash limit** |
|---|---|
| Any single organisation, except the UK Central Government | £4.0m each |
| UK Central Government | unlimited |
| Any group of organisations under the same ownership | £4.0m per group |
| Any group of pooled funds under the same management | £4.0m per manager |
| Negotiable instruments held in a broker's nominee account | £20.0m per broker |
| Foreign countries | £4.0m per country |
| Registered Providers | £4.0m in total |
| Unsecured investments with Building Societies | £4.0m in total |
| Loans to unrated corporates | £4.0m in total |
| Money Market Funds | £12.0m in total |

**Liquidity Management**: The Council uses the Logotech PSTM system, purpose-built cash flow forecasting software, to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of the Council being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Council's medium term financial plan and cash flow forecast.

# 6. Treasury Management Indicators

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

**Security:** The Council has adopted a voluntary measure of its exposure to credit risk by monitoring the value-weighted average credit score of its investment portfolio. This is calculated by applying a score to each investment (AAA=1, AA+=2, etc.) and taking the arithmetic average, weighted by the size of each investment.

| | **Target** |
|---|---|
| Portfolio average credit score | 6.0 |

**Liquidity:** The Council maintains detailed cash flow forecasts with a view to keeping minimum surplus cash balances. It addresses liquidity issues by restricting its investment opportunities to short term and instant access deposits.

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

| | **2015/16** | **2016/17** | **2017/18** |
|---|---|---|---|
| Upper limit on fixed interest rate exposure | £212.0m | £230.7m | £255.7m |
| Upper limit on variable interest rate exposure | £69.1m | £24.1m | £31.2m |

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

As a consequence of decision to borrow short, to take advantage of very low borrowing rates, the proportion of short term debt is high in 2015-16, hence the allocation to variable rate debt in early years of the forecast is higher than in previous strategies.

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

| | Upper | Lower |
|---|---|---|
| Under 12 months | 35% | 0% |
| 12 months and within 24 months | 10% | 0% |
| 24 months and within 5 years | 20% | 0% |
| 5 years and within 10 years | 50% | 0% |
| 10 years and above | 95% | 0% |

Time periods start on the first day of each financial year. The maturity date of borrowing is the earliest date on which the lender can demand repayment.

As a consequence of decision to borrow short, to take advantage of very low borrowing rates, the proportion of short term debt is high in 2015-16. This is consistent with previous strategies.

**Principal Sums Invested for Periods Longer than 364 days:** The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. The limits on the total principal sum invested to final maturities beyond the period end will be:

| | 2015/16 | 2016/17 | 2017/18 |
|---|---|---|---|
| Limit on principal invested beyond year end | £30m | £35m | £30m |

Consistent with previous strategies, the upper limit on principal invested for periods beyond 364 days allows for the investment of early surpluses on the Highways PFI contract to generate sufficient returns to cover the later years of the contract. For the first time it also allows for the longer term investment of some or all of the potential £20 million anticipated capital receipts.

# 7. Other Items

There are a number of additional items that the Council is obliged by CIPFA or CLG to include in its Treasury Management Strategy.

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

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

Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit.

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

Staff are given the opportunity to attend training courses, seminars and conferences provided by Arlingclose and CIPFA. Relevant staff are also encouraged to study professional qualifications from CIPFA, the Association of Corporate Treasurers and other appropriate organisations.

**Investment Advisers:** The Council has appointed Arlingclose Limited as treasury management advisers and receives specific advice on investment, debt and capital finance issues. The quality of this service is reviewed at an annual meeting, and advice is assessed through regular contact and meetings with the advisers throughout the year to review the outcomes of their advice.

**Investment of Money Borrowed in Advance of Need**: The Council may, from time to time, borrow in advance of need, where this is expected to provide the best long term value for money. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council's overall management of its treasury risks.

The total amount borrowed will not exceed the authorised borrowing limit of £212.0 million. The maximum period between borrowing and expenditure is expected to be two years, although the Council is not required to link particular loans with particular items of expenditure.

## 8. Financial Implications

The indicative budget for investment income from operational cash balances in 2015/16 is minimal, based on an average investment portfolio of £3.0 million at an interest rate of 0.25%.

The indicative budget for debt interest paid in 2015/16 is £6.60 million, including an average debt portfolio of £162.1 million at an average interest rate of 4.05%. These figures include the cost of borrowing for the waste project.

If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondingly different.

Specific arrangements are in place for the investment of significant capital receipts and earmarked reserves. These are budgeted and accounted for separately from operational activities, and are likely to attract significantly higher rates of return than those forecast for operational surpluses.

## 9. Other Options Considered

The CLG Guidance and the CIPFA Code do not prescribe any particular treasury management strategy for local authorities to adopt. The Head of Finance and Section 151 Officer, having consulted the members of the audit committee, believes that the above strategy represents an appropriate balance between risk management and cost effectiveness. Some alternative strategies, with their financial and risk management implications, are listed below.

| Alternative | Impact on income and expenditure | Impact on risk management |
|---|---|---|
| Invest in a narrower range of counterparties and/or for shorter times | Interest income will be lower | Lower chance of losses from credit related defaults, but any such losses will be greater |
| Invest in a wider range of counterparties and/or for longer times | Interest income will be higher | Increased risk of losses from credit related defaults, but any such losses will be smaller |
| Borrow additional sums at long-term fixed interest rates | Debt interest costs will rise; this is unlikely to be offset by higher investment income | Higher investment balance leading to a higher impact in the event of a default; however long-term interest costs will be more certain |
| Borrow short-term or variable loans instead of long-term fixed rates | Debt interest costs will initially be lower | Increases in debt interest costs will be broadly offset by rising investment income in the medium term, but long term costs will be less certain |
| Reduce level of borrowing | Saving on debt interest is likely to exceed lost investment income | Reduced investment balance leading to a lower impact in the event of a default; however long-term interest costs will be less certain |

# Appendix A – Arlingclose Limited Economic & Interest Rate Forecast – January 2015

**Underlying assumptions:**

- The UK economic recovery slowed towards the end of 2014, with economic and political uncertainty weighing on business investment. However, the Q3 growth rate of 0.7% remains slightly above the long run average, suggesting the recovery remains robust.

- Household consumption is key to the recovery in 2015. While we expect consumption growth to slow, given softening housing market activity and slower employment growth, the fall in inflation and resulting rise in both real (and nominal) wage growth and disposable income should support spending.

- Inflationary pressure is currently low (annual CPI is currently 0.5%) and is likely to remain so in the short-term. The fall in oil prices has yet to feed fully into the prices of motor fuel and retail energy and CPI is expected to fall further. Supermarket price wars are also expected to bear down on food price inflation.

- The MPC's focus is on both the degree of spare capacity in the economy and the rate at which this will be used up, factors prompting some debate on the Committee.

- Nominal earnings growth is strengthening, but remains relatively weak in historical terms, despite large falls in unemployment. Our view is that spare capacity remains extensive. The levels of part-time, self-employment and underemployment are significant and indicate capacity within the employed workforce, in addition to the still large unemployed pool. Productivity growth can therefore remain weak in the short term without creating undue inflationary pressure.

- However, we also expect employment growth to slow as economic growth decelerates. This is likely to boost productivity, which will bear down on unit labour costs and inflationary pressure.

- In addition to the lack of wage and inflationary pressures, policymakers are evidently concerned about the bleak prospects for the Eurozone. These factors will maintain the dovish stance of the MPC in the medium term. The MPC clearly believes the appropriate level for Bank Rate for the post-crisis UK economy is significantly lower than the previous norm. We would suggest this is between 2.5 and 3.5%.

- The ECB has introduced outright QE as expected. While this may alleviate some of the anxiety about the economic potential of the Eurozone, political risk remains significant (e.g. Greek election). Therefore fears for the Eurozone are likely to maintain a safe haven bid for UK government debt.

**Forecast:**

- Arlingclose continue to forecast the first rise in official interest rates in Q3 2015, but the risks to this forecast are very much weighted to the downside. The February Inflation Report will be key to our review of the possible path for Bank Rate.

- We project a slow rise in Bank Rate. The pace of interest rate rises will be gradual and the extent of rises limited; they believe the normalised level of Bank Rate post-crisis to range between 2.5% and 3.5%.

- Market sentiment (derived from forward curves) has shifted significantly lower in the past three months; market expectations are now for a later increase in interest rates and a more muted increase in gilt yields.

- The short run path for gilt yields has flattened due to the sharp decline in inflation expectations. We project gilt yields on an upward path in the medium term.

- The short run path for gilt yields is flatter due to the deteriorating Eurozone situation. We project gilt yields on an upward path in the medium term.

| | Mar-15 | Jun-15 | Sep-15 | Dec-15 | Mar-16 | Jun-16 | Sep-16 | Dec-16 | Mar-17 | Jun-17 | Sep-17 | Dec-17 | Mar-18 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| **Official Bank Rate** | | | | | | | | | | | | | |
| Upside risk | | | | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 | 0.25 |
| Arlingclose Central Case | 0.50 | 0.50 | 0.75 | 0.75 | 1.00 | 1.00 | 1.25 | 1.25 | 1.50 | 1.50 | 1.75 | 1.75 | 1.75 |
| Downside risk | | | 0.25 | 0.25 | 0.50 | 0.50 | 0.75 | 0.75 | 1.00 | 1.00 | 1.00 | 1.00 | 1.00 |
| **3-month LIBID rate** | | | | | | | | | | | | | |
| Upside risk | 0.10 | 0.20 | 0.20 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 |
| Arlingclose Central Case | 0.55 | 0.60 | 0.80 | 0.90 | 1.05 | 1.15 | 1.30 | 1.40 | 1.55 | 1.65 | 1.80 | 1.95 | 2.00 |
| Downside risk | 0.15 | 0.20 | 0.30 | 0.40 | 0.55 | 0.65 | 0.75 | 0.85 | 0.95 | 0.95 | 0.95 | 0.95 | 1.00 |
| **1-yr LIBID rate** | | | | | | | | | | | | | |
| Upside risk | 0.10 | 0.20 | 0.20 | 0.30 | 0.30 | 0.30 | 0.30 | 0.30 | 0.40 | 0.40 | 0.40 | 0.40 | 0.40 |
| Arlingclose Central Case | 0.95 | 1.00 | 1.20 | 1.30 | 1.45 | 1.55 | 1.70 | 1.80 | 1.95 | 2.05 | 2.20 | 2.35 | 2.40 |
| Downside risk | 0.15 | 0.20 | 0.30 | 0.50 | 0.55 | 0.60 | 0.65 | 0.70 | 0.75 | 0.80 | 0.80 | 0.80 | 0.80 |
| **5-yr gilt yield** | | | | | | | | | | | | | |
| Upside risk | 0.35 | 0.40 | 0.40 | 0.40 | 0.40 | 0.40 | 0.40 | 0.45 | 0.45 | 0.45 | 0.45 | 0.50 | 0.50 |
| Arlingclose Central Case | 1.10 | 1.20 | 1.30 | 1.40 | 1.50 | 1.65 | 1.80 | 1.95 | 2.10 | 2.20 | 2.35 | 2.40 | 2.50 |
| Downside risk | 0.35 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.55 | 0.60 | 0.65 | 0.70 | 0.70 | 0.70 | 0.75 |
| **10-yr gilt yield** | | | | | | | | | | | | | |
| Upside risk | 0.35 | 0.40 | 0.40 | 0.40 | 0.40 | 0.45 | 0.45 | 0.45 | 0.45 | 0.50 | 0.50 | 0.55 | 0.55 |
| Arlingclose Central Case | 1.60 | 1.70 | 1.80 | 1.90 | 2.00 | 2.15 | 2.30 | 2.45 | 2.60 | 2.70 | 2.85 | 2.90 | 3.00 |
| Downside risk | 0.35 | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.55 | 0.60 | 0.65 | 0.70 | 0.70 | 0.75 | 0.80 |
| **20-yr gilt yield** | | | | | | | | | | | | | |
| Upside risk | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 | 0.55 |
| Arlingclose Central Case | 2.10 | 2.20 | 2.30 | 2.35 | 2.45 | 2.50 | 2.65 | 2.75 | 2.90 | 3.00 | 3.15 | 3.20 | 3.30 |
| Downside risk | 0.35 | 0.40 | 0.50 | 0.60 | 0.70 | 0.75 | 0.75 | 0.75 | 0.80 | 0.85 | 0.85 | 0.90 | 0.90 |
| **50-yr gilt yield** | | | | | | | | | | | | | |
| Upside risk | 0.35 | 0.40 | 0.45 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.50 | 0.55 | 0.55 | 0.55 | 0.55 |
| Arlingclose Central Case | 2.15 | 2.25 | 2.35 | 2.40 | 2.50 | 2.55 | 2.70 | 2.80 | 2.95 | 3.05 | 3.20 | 3.25 | 3.35 |
| Downside risk | 0.35 | 0.40 | 0.50 | 0.60 | 0.70 | 0.75 | 0.75 | 0.75 | 0.80 | 0.85 | 0.85 | 0.90 | 0.90 |

# Appendix B – Existing Investment & Debt Portfolio Position

| | 31 August 2015 **Actual Portfolio £m** | 31 August 2015 **Average Rate %** |
|---|---|---|
| **External Borrowing:** | | |
| PWLB – Fixed Rate | 104.4 | 5.17 |
| PWLB – Variable Rate | 5.0 | 5.10 |
| Local Authorities | 5.0 | 1.15 |
| LOBO Loans | 5.0 | 4.27 |
| **Total External Borrowing** | **119.4** | **4.96** |
| **Other Long Term Liabilities:** | | |
| PFI | 43.7 | |
| Finance Leases | 0.8 | |
| **Total Gross External Debt** | **163.9** | |
| **Investments:** | | |
| *Managed in-house* | | |
| Short-term investments | 4.5 | 0.57 |
| *Managed externally* | | |
| Pooled Funds (Money Market Funds) | 0.0 | 0.00 |
| **Total Investments** | **4.5** | **0.57** |
| **Net Debt** | **159.4** | |

# Appendix C – Prudential Indicators 2015/16

The Local Government Act 2003 requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy's *Prudential Code for Capital Finance in Local Authorities* (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice. To demonstrate that the Council has fulfilled these objectives, the Prudential Code sets out the following indicators that must be set and monitored each year.

**Estimates of Capital Expenditure:** The Council's planned capital expenditure and financing, including additional capital expenditure approved at Executive on 15 September 2015 and Waste contract budgets, may be summarised as follows.

| Capital Expenditure and Financing | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|
| **Total Expenditure** | **17.6** | **39.0** | **22.7** | **48.6** |
| Capital Receipts | 1.8 | 2.5 | 0.5 | 0.5 |
| Government Grants | 9.4 | 13.5 | 3.1 | 3.1 |
| Reserves | 0.0 | 0.0 | 0.0 | 0.0 |
| Revenue | 0.3 | 0.0 | 0.0 | 0.0 |
| Borrowing | 6.1 | 23.0 | 19.1 | 45.0 |
| Leasing and PFI | 0.0 | 0.0 | 0.0 | 0.0 |
| **Total Financing** | **17.6** | **39.0** | **22.7** | **48.6** |

**Estimates of Capital Financing Requirement:** The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose.

| Capital Financing Requirement | 31.03.15 Actual £m | 31.03.16 Estimate £m | 31.03.17 Estimate £m | 31.03.18 Estimate £m |
|---|---|---|---|---|
| **Total CFR** | **247.3** | **280.2** | **315.6** | **357.3** |

The CFR is forecast to rise by £110.0m over the next three years due to significant investment from the waste contract, and as historic capital expenditure financed by debt outweighs resources put aside for debt repayment, principally as a result of the Highways PFI project.

**Gross Debt and the Capital Financing Requirement:** In order to ensure that over the medium term debt will only be for a capital purpose, the Council should ensure that debt does not, except in the short term, exceed the total of capital financing requirement in the preceding year plus the estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence.

| Debt | 31.03.15 Revised £m | 31.03.16 Estimate £m | 31.03.17 Estimate £m | 31.03.18 Estimate £m |
|---|---|---|---|---|
| Borrowing | 160.3 | 173.6 | 180.8 | 208.9 |
| Finance leases | 0.9 | 0.4 | 0.2 | 0.2 |
| PFI liabilities | 49.7 | 67.8 | 84.7 | 101.4 |
| **Total Debt** | **210.9** | **241.8** | **265.7** | **310.5** |

Total debt is expected to remain below the CFR during the forecast period.

**Operational Boundary for External Debt:** The operational boundary is based on the Council's estimate of most likely (i.e. prudent but not worst case) scenario for external debt. It links directly to the Council's estimates of capital expenditure, the capital financing requirement and cash flow requirements, and is a key management tool for in-year monitoring. Other long-term liabilities comprise finance lease, Private Finance Initiative and other liabilities that are not borrowing but form part of the Council's debt.

| Operational Boundary | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|
| Borrowing | 160.0 | **185.0** | 190.0 | 220.0 |
| Other long-term liabilities | 51.0 | **68.0** | 85.0 | 102.0 |
| **Total Debt** | **201.0** | **253.0** | **275.0** | **322.0** |

**Authorised Limit for External Debt:** The authorised limit is the affordable borrowing limit determined in compliance with the Local Government Act 2003. It is the maximum amount of debt that the Council can legally owe. The authorised limit provides headroom over and above the operational boundary for unusual cash movements.

| Authorised Limit | 2014/15 Revised £m | 2015/16 Estimate £m | 2016/17 Estimate £m | 2017/18 Estimate £m |
|---|---|---|---|---|
| Borrowing | 197.0 | **212.0** | 231.0 | 256.0 |
| Other long-term liabilities | 51.0 | **68.0** | 85.0 | 102.0 |
| **Total Debt** | **248.0** | **280.0** | **316.0** | **358.0** |

**Ratio of Financing Costs to Net Revenue Stream:** This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet financing costs, net of investment income.

| Ratio of Financing Costs to Net Revenue Stream | 2014/15 Revised % | 2015/16 Estimate % | 2016/17 Estimate % | 2017/18 Estimate % |
|---|---|---|---|---|
| General Fund | 12.4 | **14.1** | 15.6 | 17.3 |

**Incremental Impact of Capital Investment Decisions:** This is an indicator of affordability that shows the impact of capital investment decisions on Council Tax levels. The incremental impact is the difference between the total revenue budget requirement of the current approved capital programme and the revenue budget requirement arising from the capital programme proposed.

| Incremental Impact of Capital Investment Decisions | 2015/16 Estimate £ | 2016/17 Estimate £ | 2017/18 Estimate £ |
|---|---|---|---|
| General Fund - increase in annual band D Council Tax | **0.19** | 2.18 | 6.02 |

The ratio above in respect of the impact of additional borrowing on Council Tax charges is purely illustrative. Should the cost of borrowing increase, the additional costs would have to be funded through savings in other areas, rather than being passed directly to Council Tax-payers.

The key focus of the treasury management strategy, and the associated prudential indicators, is to ensure that the council's commitments within its capital programme are prudently and affordably financed, without disadvantaging other areas of service delivery.

**Adoption of the CIPFA Treasury Management Code:** The Council adopted the Chartered Institute of Public Finance and Accountancy's *Treasury Management in the Public Services: Code of Practice 2011 Edition* in February 2003.

# Appendix D – Annual Minimum Revenue Provision Statement 2015/16

Where the Council finances capital expenditure by debt, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP), although there has been no statutory minimum since 2008. The Local Government Act 2003 requires the Council to have regard to the Department for Communities and Local Government's *Guidance on Minimum Revenue Provision* (the CLG Guidance) most recently issued in 2012.

The broad aim of the CLG Guidance is to ensure that debt is repaid over a period that is either reasonably commensurate with that over which the capital expenditure provides benefits, or, in the case of borrowing supported by Government Revenue Support Grant, reasonably commensurate with the period implicit in the determination of that grant.

The CLG Guidance requires the Council to approve an Annual MRP Statement each year, and recommends a number of options for calculating a prudent amount of MRP. The following statement incorporates options recommended in the Guidance as well as locally determined prudent methods.

- For capital expenditure incurred before 1 April 2008 MRP will be determined as 2% of the Capital Financing Requirement in respect of that expenditure.

- For capital expenditure incurred after 31 March 2008, MRP will be determined by charging the expenditure over the expected useful life of the relevant assets in equal instalments, starting in the year after the asset becomes operational. MRP on purchases of freehold land will be charged over 50 years. MRP on expenditure not related to fixed assets but which has been capitalised by regulation or direction will be charged over a maximum period of 20 years.

- For loans to other bodies incurred after 31 March 2008 will increase the councils CFR. The repayment is set aside as a capital receipt so no MRP liability will be recognised in the accounts. Where a default occurs the council will be required to make an MRP charge to the amount of the total default.

- For assets acquired by finance leases or the Private Finance Initiative, MRP will be determined as being equal to the element of the rent or charge that goes to write down the balance sheet liability. However the council reserves the right to choose an alternative approach so long as it can demonstrate it is making a prudent provision each year under the capital accounting regulations.

Capital expenditure incurred during 2015/16 will not be subject to a MRP charge until 2016/17.

Based on the Council's latest estimate of its Capital Financing Requirement on 31 March 2015, the budget for MRP has been set as follows:

| | **31.03.2015 Estimated CFR £m** | **2015/16 Estimated MRP £** |
|---|---|---|
| Capital expenditure before 01.04.2008 | **127.0** | 2.5 |
| Capital expenditure after 31.03.2008 | **67.8** | 2.9 |
| Finance leases and Private Finance Initiative | **50.6** | 2.9 |
| Transferred debt | **0** | 0 |
| Loans to other bodies | **1.9** | 0 |
| **Total General Fund** | **247.3** | **8.3** |

# Appendix E – Treasury Management Practices (TMPs)

**TMP1 – Risk management**
The Head of Finance and Section 151 Officer will design, implement and monitor all arrangements for the identification, management and control of treasury management risk, will report at least annually on the adequacy/suitability thereof, and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the council's objectives in this respect, all in accordance with the procedures set out in *TMP6 – Reporting requirements and management information arrangements.*

In respect of each of the following risks, the arrangements which seek to ensure compliance with these objectives are set out in the schedules to this document.

**TMP1[1] Credit and counterparty risk management**
The council regards a key objective of its treasury management activities to be the security of the principal sums it invests. Accordingly, it will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with which funds may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in *TMP4 – Approved instruments, methods and techniques* and listed in section 5 of this strategy document. It also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing arrangements.

**TMP1[2] Liquidity risk management**
The council will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives.

The council will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.

**TMP1[3] Interest rate risk management**
The council will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with *TMP6 – Reporting requirements and management information arrangements*.

It will achieve this by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates. This should be the subject to the consideration and, if required, approval of any policy or budgetary implications.

It will ensure that any hedging tools, such as derivatives are only used for the management of risk and the prudent management of financial affairs and that the policy for the use of derivatives is clearly detailed in the annual strategy.

**TMP1[4] Exchange rate risk management**
The council will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income/expenditure levels.

**TMP1[5] Refinancing risk management**
The council will ensure that its borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the council as can reasonably be achieved in the light of market conditions prevailing at the time.

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid over-reliance on any one source of funding if this might jeopardise achievement of the above.

**TMP1[6] Legal and regulatory risk management**
The council will ensure that all of its treasury management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counterparty policy under *TMP1[1] Credit and counterparty risk management*, it will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the council, particularly with regard to duty of care and fees charged.

The council recognises that future legislative or regulatory changes may impact on its treasury management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the council.

**TMP1[7] Fraud, error and corruption, and contingency management**
The council will ensure that it has identified the circumstances which may expose it to the risk of loss through fraud, error, corruption or other eventualities in its treasury management dealings. Accordingly, it will employ suitable systems and procedures, and will maintain effective contingency management arrangements, to these ends.

**TMP1[8] Market risk management**
The council will seek to ensure that its stated treasury management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests, and will accordingly seek to protect itself from the effects of such fluctuations.

**TMP2 – Performance measurement**
The council is committed to the pursuit of value for money in its treasury management activities, and to the use of performance methodology in support of that aim, within the framework set out in its treasury management policy statement.

Accordingly, the treasury management function will be the subject of on-going analysis of the value it adds in support of the council's stated business or service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal or other grant or subsidy incentives, and of the scope for other potential improvements.

Treasury management performance measures are included in the Financial Management mini service board report from CorBusiness.

On a quarterly basis, the treasury management function reports on:

- Actual external borrowing compared to the authorised and operational limits agreed in the prudential indictors.
- Actual interest rate exposure compared to the upper limits agreed in the Prudential Indicators.

Annually, the treasury management function reports on

- The average cost of long term debt – ensuring that the borrowings made minimise costs to the council.
- The affordability measures concerning the cost of borrowing as contained in the Prudential Indicators.
- The difference between actual external borrowing and the Capital Financing Requirement.

These performance measures are reported to the Financial Management mini service board meeting, and are included in the reports made to audit committee throughout the year.

The council also subscribes to the CIPFA Treasury Management Benchmarking Club, which enables comparison of the council's performance to other local authorities, in terms of interest payable and receivable, investment performance, borrowing requirements and maturity profiles, and the costs of carrying out treasury management activities.

**TMP3 – Decision-making and analysis**

The council will maintain full records of its treasury management decisions, and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time.

The Head of Finance and Section 151 Officer is responsible for treasury management decisions.

On a daily basis, decisions regarding investments of short term cash surpluses are made by the Treasury Management Assistant, and reviewed and approved by the Technical Finance Officer.

A monthly Treasury Management Group meeting is held to make decisions regarding borrowing requirements, changes to the approved lending and borrowing lists, and any other strategic treasury management decisions. The members of the Treasury Management Group are the Head of Finance and Section 151 Officer, the Finance Manager, the Technical Finance Officer and three Principal Accountants. Notes of these meetings are taken to support decisions made.

Any changes to the Treasury Management Strategy made throughout the year will be reported to the audit committee.

**TMP4 – Approved instruments, methods and techniques**

The council will undertake its treasury management activities by employing only those instruments, methods and techniques detailed in this document, and within the limits and parameters defined in *TMP1 – Risk management.*

Where the council intends to use derivative instruments for the management of risks, these will be limited to those set out in its annual treasury strategy. The council will seek proper advice and will consider that advice when entering into arrangements to use such products to ensure that it fully understands those products.

**TMP5 – Organisation, clarity and segregation of responsibilities, and dealing arrangements**

The council considers it essential, for the purposes of the effective control and monitoring of its treasury management activities, for the reduction of the risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times a clarity of treasury management responsibilities.

The principle on which this will be based is a clear distinction between those charged with setting treasury management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of treasury management decisions, and the audit and review of the treasury management function.

If and when the council intends, as a result of lack of resources or other circumstances, to depart from these principles, the Head of Finance and Section 151 Officer will ensure that the reasons are properly reported in accordance with *TMP6 – Reporting requirements and management information arrangements*, and the implications properly considered and evaluated.

The Head of Finance and Section 151 Officer will ensure that there are clear written statements of the responsibilities for each post engaged in treasury management, and the arrangements for absence cover. The Head of Finance and Section 151 Officer will also ensure that at all times those engaged in treasury management will follow the policies and procedures set out.

The Head of Finance and Section 151 Officer will ensure there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds.

The delegations to the Head of Finance and Section 151 Officer in respect of treasury management are set out in the council's Constitution. The Head of Finance and Section 151 Officer will fulfil all such responsibilities in accordance with the council's policy statement and TMPs and, if a CIPFA member, the Standard of Professional Practice on Treasury Management.

**TMP6 – Reporting requirements and management information arrangements**

The council will ensure that regular reports are prepared and considered on the implementation of its treasury management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; on the implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its treasury management activities; and on the performance of the treasury management function.

As a minimum the audit committee will receive:

- an annual report on the strategy and plan to be pursued in the coming year
- a mid-year review
- an annual report on the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the council's treasury management policy statement and TMPs.

The full council will receive and approve the annual strategy and plan to be pursued in the coming year, as part of the council's budget strategy.

The audit committee will receive regular monitoring reports on treasury management activities and risks.

The audit committee will have responsibility for the scrutiny of treasury management policies and practices.

Local authorities should report the treasury management indicators as detailed in their sector-specific guidance notes.

**TMP7 – Budgeting, accounting and audit arrangements**

The Head of Finance and Section 151 Officer will prepare, and the council will approve and, if necessary, from time to time will amend, an annual budget for treasury management, which will bring together all of the costs involved in running the treasury management function, together with associated income. The matters to be included in the budget will at minimum be those required by statute or regulation, together with such information as will demonstrate compliance with *TMP1 – Risk management*, *TMP2 – Performance measurement*, and *TMP4 – Approved instruments, methods and techniques*.

The Head of Finance and Section 151 Officer will exercise effective controls over this budget, and will report upon and recommend any changes required in accordance with *TMP6 – Reporting requirements and management information arrangements*. The council will account for its treasury management activities, for decisions made and transactions executed, in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

**TMP8 – Cash and cash flow management**

Unless statutory or regulatory requirements demand otherwise, all monies in the hands of the council will be under the control of Head of Finance and Section 151 Officer, and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis, and the Head of Finance and Section 151 Officer will ensure that these are adequate for the purposes of monitoring compliance with *TMP1[2] Liquidity risk management*.

The council uses the Logotech Public Sector Treasury Management (PSTM) system for recording cash flow movements and creating cash flow forecasts.

Daily cash flow activities are recorded on the system and the daily bank balances reconciled.

Cash flow forecasts, based on historic activity and current year budget assumptions, are prepared at the start of each financial year, and are discussed at the monthly treasury management meetings detailed under *TMP3 – Decision-making and analysis* above.

**TMP9 – Money laundering**

The council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. Accordingly, it will maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that staff involved in this are properly trained.

The council's Anti-Money Laundering Policy sets out the council's procedures to prevent the use of council services for money laundering purposes, including the name of the officer to whom reports should be made.

**TMP10 – Training and qualifications**

The council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Head of Finance and Section 151 Officer will recommend and implement the necessary arrangements.

The Head of Finance and Section 151 Officer will ensure that council members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.

Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

**TMP11 – Use of external service providers**

The council recognises that responsibility for treasury management decisions remains with the council at all times. It recognises that there may be potential value in employing external providers of treasury management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will ensure it does so for reasons which have been submitted to a full evaluation of the costs and benefits. It will also ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review. And it will ensure, where feasible and necessary, that a spread of service providers is used, to avoid over-reliance on one or a small number of companies. Where services are subject to formal tender or re-tender arrangements, legislative requirements will always be observed. The monitoring of such arrangements rests with the Head of Finance and Section 151 Officer.

**TMP12 – Corporate governance**

The council is committed to the pursuit of proper corporate governance throughout its businesses and services, and to establishing the principles and practices by which this can be achieved. Accordingly, the treasury management function and its activities will be undertaken with openness and transparency, honesty, integrity and accountability.

The council has adopted and has implemented the key principles of the Code. This, together with the other arrangements detailed in the schedules to this document, are considered vital to the achievement of proper corporate governance in treasury management, and the Head of Finance and Section 151 Officer will monitor and, if and when necessary, report upon the effectiveness of these arrangements.