



PAPER G

Purpose: For Decision / Noting

Committee report

Committee	AUDIT COMMITTEE
Date	13 MARCH 2017
Title	TREASURY MANAGEMENT STRATEGY 2017-18
Report of	PENSION FUND AND TREASURY MANAGEMENT ACCOUNTANT

EXECUTIVE SUMMARY

1. This report presents the Treasury Management Strategy 2017-18. The strategy forms part of the council's overall annual budget strategy.
2. The committee is asked to agree the Treasury Management Strategy for 2017-18, for onward approval by full council.

BACKGROUND

3. The Local Government Act 2003 and subsequent regulations require the council to set out its annual strategy with regard to both borrowing and the repayment of external debt. These are set out in the Borrowing Strategy (Section 4 of the attached Treasury Management Strategy Statement) and the Minimum Revenue Provision (MRP) Statement (Appendix D of the attached Treasury Management Strategy Statement) respectively.
4. The Act and subsequent regulations require the council to have regard to the Chartered Institute of Public Finance and Accountancy's (CIPFA's) revised Code of Practice for Treasury Management ("the Code"), and Treasury Management Practices ("TMPs"); the council is also required to have regard to the CIPFA Prudential Code for Capital Finance ("the Prudential Code") and to set prudential indicators for the next three years to ensure that the council's investment plans are affordable, prudent and sustainable. With regard to its investment plans the council also has a duty to determine a prudent MRP.
5. The council must also approve an annual Investment Strategy in compliance with government guidance on local government investments. Section 5 of the attached Treasury Management Strategy Statement sets out the council's policy for managing its investments and for giving priority to the security and liquidity of those investments.

6. The council's TMPs, included in Appendix E of the attached Treasury Management Strategy Statement, sets out how the council proposes to achieve its stated policy objectives, and how it will manage and control its treasury management activities. The TMPs specifically cover the following areas:
 - TMP 1 – Risk management
 - TMP 2 – Performance measurement
 - TMP 3 – Decision making and analysis
 - TMP 4 – Approved Instruments, methods and techniques
 - TMP 5 – Organisation, clarity and segregation of responsibilities, and dealing arrangements
 - TMP 6 – Reporting requirements and management information arrangements
 - TMP 7 – Budgeting, accounting and audit arrangements
 - TMP 8 – Cash and cash flow management
 - TMP 9 – Money laundering
 - TMP 10 – Training and qualifications
 - TMP 11 – Use of external service providers
 - TMP 12 – Corporate governance
7. 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. The framework requires that the council sets and monitors its performance against a set of prudential indicators which are designed to support and record local decision making in these key areas.
8. The prudential indicators, included in Appendix C of the attached Treasury Management Strategy Statement, are intended to ensure that decisions concerning capital expenditure, debt and treasury management are both affordable and prudent.

STRATEGIC CONTEXT

9. The Treasury Management Strategy forms part of the council's overall budget strategy, specifically supporting the latest [Corporate Plan 2015-17](#), under priority 4: Ensuring that all the resources available to the Island are used in the most effective way in achieving the Island's priorities
10. The strategy specifically supports the council's capital programme and the Medium Term Financial Strategy, ensuring the key priorities of the council are deliverable within the reduced resources available to the council.

CONSULTATION

11. The draft strategy has been prepared in conjunction with advice received from the council's treasury management advisers, Arlingclose Limited, who have provided details of the external economic context and have reviewed the draft strategy for compliance with regulations, etc.

FINANCIAL / BUDGET IMPLICATIONS

12. The Council's Medium Term Financial Strategy approved in October 2016, set out the case for changing the Council's current MRP policy. It was aimed at increasing the Council's financial capacity and therefore is operational capacity to implement change over a more manageable period. To achieve this, the Annuity Method as the methodology for setting aside a "prudent amount" for the provision for debt repayment from 2016/17 was approved. This has the effect of securing savings commencing at £2m per annum and provides the ability to release £39.6m of "overprovision" of MRP to support the Council's new Medium Term Financial Strategy.
13. In practice, the change to the Annuity Method allows the Council to take a "Debt Repayment holiday" for the next 5 years in order to draw down on the "overprovision" for funding debt liabilities at sums between £7m to £8m per annum with the consequent effect of "smoothing out" the necessary savings, allowing more time for transformation plans and initiatives to improve funding / income generation to take effect
14. There are no other direct financial or budgetary implications arising from the review of the Treasury Management Strategy and policy. However, the establishment of effective arrangements for the regular monitoring and review of the council's treasury management arrangements and prudential indicators is a key part of the effective financial management of the council.
15. The indicative budget for investment income in 2017-18 is £0.16 million, and this is based on an average investment portfolio of £38.3 million at an interest rate of 0.41 per cent.
16. The indicative budget for debt interest paid in 2017-18 is £7.5 million. The cash flows, on which this strategy is based, include an average debt portfolio of £170.7 million at an average interest rate of 4.4 per cent.
17. If actual levels of investments and borrowing, and actual interest rates differ from those forecast, performance against budget will be correspondingly different.

LEGAL IMPLICATIONS

18. The Local Government Act 2003 and subsequent regulations require the council to set out its annual strategy with regard to both borrowing and the repayment of external debt. The Act and subsequent regulations require the council to have regard to CIPFA's revised Code of Practice for Treasury

Management in Local Authorities, and TMPs. The council is also required to have regard to the CIPFA Prudential Code for Capital Finance, and to set prudential indicators for the next three years to ensure the council's investment plans are affordable, prudent and sustainable.

EQUALITY AND DIVERSITY

19. The council has a legal duty under the Equality Act 2010 to seek to eliminate discrimination, victimisation and harassment in relation to age, disability, gender reassignment, pregnancy and maternity, race, religion, sex, sexual orientation and marriage and civil partnerships. The treasury management strategy is not considered to have any impacts upon the equality duties.

RISK MANAGEMENT

20. Treasury management activities have a high level of risk in that they relate to transactions that can amount to several million pounds which are undertaken with external bodies. When the council has surplus monies to invest, there are risks if those organisations to whom it lends default on repayment. The costs to the council of its treasury management activities are dependent on fluctuating interest rates.
21. The overall strategy of borrowing short-term and avoiding long-term debt carries the risk that, if interest rates suddenly rise, when longer term debt is eventually required, it will cost more.
22. The council manages these risks by adopting a treasury management strategy which includes a statement of treasury management practice specifically relating to risk, covering the following risk areas:
 - Credit and counterparty risk – who the council is permitted to lend to and borrow from and what instruments it can utilise
 - Liquidity risk – ensuring that sufficient, but not excessive, funds are available when needed
 - Interest rate risk – minimising the council's exposure to significant fluctuations in interest rates, both investment income and borrowing costs, by continually reviewing the instruments it uses
 - Exchange rate risk – minimising the council's exposure to foreign exchange risk by restricting the exposure to foreign currency investments and overseas counterparties
 - Refinancing risk – ensuring that the maturity profile of long term debt is as evenly spread as possible, and planning for the replacement of maturing debt at the most favourable interest rates
 - Legal and regulatory risk – ensuring compliance with regulations and statutory requirements
 - Risk of fraud, error and corruption – ensuring that appropriate controls are in place around staffing and processes, and ensuring appropriate business continuity arrangements exist

- Market risk – ensuring that the council’s treasury management activities are not compromised by adverse economic circumstances.
23. The committee’s overview of the council’s treasury management arrangements plays an important part in the council’s overall governance regime. It has an important role to play in the monitoring of treasury management activities, including overview of the risks faced by this function both internally, which are directly controllable through segregation of duties and reporting arrangements, and externally, controllable through the monitoring of counterparties and lending limits, and also regular monitoring of general economic factors.

RECOMMENDATION

24. That the council be recommended to agree the following changes to the 2016-17 Treasury Management Strategy:
- (i) that the minimum revenue provision for the repayment of government supported borrowing, other than finance leases and service concessions (including private finance initiative schemes) is changed from a straight 2% annual provision to a 50 year annuity provision with effect from 2016-17 (paragraph 4 Appendix D of Treasury Management Strategy).
 - (ii) that with regard to capital expenditure loans to third parties the principal element of the repayment is set aside to repay the borrowing that has financed these assets (paragraph 6 Appendix D of Treasury Management Strategy)
 - (iii) that with regard to the purchase of investment properties – such properties will be disposed of before there is a significant consumption of the asset, and that the council provides for the repayment of the borrowing undertaken for their purchase by setting aside the capital receipt on their disposal rather than providing a revenue provision.
 - (iv) that the maximum investment in a single Local Authority will be increased from £4m to £10m
 - (v) that the maximum investment that can be made into any one organisation (other than the UK Government including Local Authorities) be increased from £4m to £8m
25. That the council be recommended to agree the Treasury Management Strategy for 2017-18.

APPENDICES ATTACHED

26. [Appendix](#) – Treasury Management Strategy 2017-18

BACKGROUND PAPERS

- CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (2011 Edition)
http://www.tisonline.net/investments/content/Treasury_Code_2011.pdf
- CIPFA The Prudential Code for Capital Finance in Local Authorities (2011 Edition)
http://www.tisonline.net/localauthorityaccounting/content/Prudential_Code_2011.pdf

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