GOVERNANCE AND AUDIT COMMITTEE
29 MARCH 2010

TREASURY MANAGEMENT REPORT
(Borough Treasurer)

1 PURPOSE OF DECISION

1.1 The purpose of this report is to satisfy the new requirement contained within the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code of Practice to have a nominated responsible body, being the Governance and Audit Committee, examine and assess the effectiveness of the Council's treasury management strategy and polices.

2 RECOMMENDATION(S)

2.1 That the committee specifically consider

- **The Capital Prudential Indicators and Limits for 2010/11 to 2012/13 contained within Annex A**
- **The Minimum Revenue Provision Policy contained within Annex B**
- **The Treasury Management Strategy Statement and the Treasury Prudential Indicators contained in Annex C**
- **The Authorised Limit Prudential Indicator contained in Annex C**
- **The Investment Strategy 2010/11 to 2012/13 and Treasury Management Limits on Activity contained in Annex D**
- **The Treasury Policy Statement contained in Annex F**

3 ADVICE RECEIVED FROM STATUTORY AND OTHER OFFICERS

<u>Borough Solicitor</u>

3.1 Nothing to add to the report.

<u>Borough Treasurer</u>

3.2 Interest rates reflect the risk associated with investments and there can be no absolute guarantee for any investment. However the Council has sought in the past to protect the return of capital wherever possible. The Government has issued a consultation on new guidance on treasury management and this report incorporates those recommendations.

<u>Equalities Impact Assessment</u>

3.3 None Required

<u>Strategic Risk Management Issues</u>

3.4 The report and attached Annexes deal directly with the strategic management of risk associated with the treasury management service of the authority.

4 SUPPORTING INFORMATION

Treasury Management

4.1 The Code of Practice defines treasury management as:

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

4.2 The Local Government Act 2003 requires a local authority to "have regard (a) to such guidance as the Secretary of State may issue, and (b) to such other guidance as the Secretary of State may by regulations specify".

4.3 The guidance issued by the Communities and Local Government (CLG) is currently under consultation however the key principles outlined in the consultation document are likely to be upheld.

4.4 Two Codes of Practice issued by CIPFA (CIPFA Prudential Code and CIPFA Treasury Management Code of Practice (the Code)) contain investment guidance which compliments the CLG Guidance and as such Local Authorities are required to have regard to these Codes. These were revised in November 2009 with a key change of increasing Members responsibility in this area, particularly in the examinations and assessment of the effectiveness of the treasury management strategy and policies.

4.5 The Code recommends that a responsible body be nominated by the Council and having examined and assessed the effectiveness of the treasury management strategy and polices recommend them to Council. However the new legislation and guidance was issued very late in the budget cycle and as such Council approved the necessary strategies and policies at its meeting on March 3rd and nominated the Governance and Audit Committee as the responsible body. The intention was for the Governance and Audit Committee to review these strategies and policies and to have the opportunity to report back as part of the mid-year review of the Council's treasury management activities.

4.6 Going forward it will be necessary to bring forward the timing of these strategies and policies to ensure that the Governance and Audit Committee have sufficient time to assess the effectiveness of the treasury management activities of the Council before recommending the strategies and policies to the Executive and Council as part of the normal budget cycle.

CLG Guidance and CIPFA Code of Practice

4.7 In light of the banking crisis in 2008 and the continued economic uncertainty, CIPFA has amended the Code of Practice. It is a requirement of the Council to adopt the revised Code and the Treasury Policy Statement. The revised Code has emphasised a number of key areas.

- The strategy report will affirm that the effective management and control of risk are prime objectives of the Council's treasury management activities.
- The Council's appetite for risk must be clearly identified within the strategy report and will affirm that priority is given to security of capital and liquidity when investing funds and explain how this will be carried out.

- Responsibility for risk management and control lies within the organisation and cannot be delegated to any outside organisation.
- Credit ratings should only be used as a starting point when considering risk.
- Borrowing in advance of need is only permissible where there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities.
- There should be a mid-year review of treasury management strategy and performance to highlight any areas of concern since the original strategy was approved.
- Each Council must delegate the role of assessing the effectiveness of the treasury management strategy and policies to a specific named body.

4.8 The Council is required under Section 15 of the Local Government Act 2003 to approve an Annual Investment and Treasury Management Strategy before the start of each year. These reports fulfil four key legislative requirements;

- The reporting of the Prudential Indicators setting out the expected capital activities.
- Setting out the Council's Minimum Revenue Provision (MRP) Policy outlining how the Council will pay for capital assets through revenue each year.
- The Treasury Management Strategy Statement which sets out how the Council's treasury service will support the capital decisions taken above, the day to day treasury management and the limitations on activity through treasury prudential indicators.
- The Annual Investment Strategy which sets out the Council's criteria for choosing investment counterparties and limiting exposure to the risk of loss.

4.9 Each of these areas is examined in more detail below.

<u>Capital Prudential Indicators</u>

4.10 The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code and produce prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity. The key indicators are

- The Council's capital expenditure plans
- The Council's borrowing need – Capital Finance Requirement (CFR)
- Ratio of financing costs to net-revenue stream
- Incremental impact of capital investment on Council Tax

4.11 These are attached in Annex A

<u>Minimum Revenue Provision (MRP)</u>

4.12 The concept of the MRP was introduced as part of the change to the Local Government Capital Finance System in April 1990. This required local authorities to assess their outstanding debt and to make an annual charge to revenue through the General Fund. The broad aim of a prudent provision is to ensure that the debt is repaid over a period which is reasonably commensurate with that over which the capital expenditure provides benefits. It is a requirement that Council approve an annual MRP Statement. This is attached in Annex B.

Treasury Management Strategy

4.13 The Treasury Management Strategy is an important part of the overall financial management of the Council's affairs. The Council's treasury activities are strictly regulated by statutory requirements and a professional Code of Practice. The Code requires an annual strategy to be reported to Council outlining the expected treasury activity and explaining both the risk and the management of the risks, associated with the treasury service.

4.14 This strategy covers:

- The Council's debt and investment projections.
- The Council's estimates and limits on future debt levels.
- The expected movement in interest rates.
- The Council's borrowing and investment strategies.
- Treasury performance indicators.
- Specific limits on treasury activities.

4.15 The Treasury Management Strategy for 2010/11 is attached in Annex C

Investment Strategy

4.16 The Council's investment strategy primary objectives are safeguarding the repayment of the principal and interest of its investments first and ensuring adequate liquidity second – the investment return being a less important objective. This is consistent with the Council's approach to investments in the past. However the revenue impact of interest is not insignificant. Even though it is a lower priority it is an important component of the Council medium term financial strategy.

4.17 The current investment climate has one over-riding risk consideration – that of counterparty security risk. The Investment Strategy for 2010/11, attached in Annex D, sets out the category of investment types the Council will invest in, and the criteria for choosing investment counterparties.

4.18 The Borough Treasurer will maintain a counterparty list in compliance with the criteria laid out in the Investment Strategy. This rating criteria use the "lowest common denominator" approach of selecting counterparties. For example if an institution is rated by two rating agencies, one meets the Council's criteria, the other does not, then the institution will fall outside the lending criteria.

4.19 In accordance with CLG guidance, the Council will, in considering the security of proposed investments, follow different procedures according to which two categories, Specified or Unspecified, the investment falls into.

4.20 Specified investments offer high security and high liquidity and are deemed to be;

- Denominated in Sterling
- Not long term investments (ie less than 365 days)
- Have a high credit rating or are made with the UK Government or other Local Authority

4.21 An over-riding investment limit of 364 days has been approved as part of the Investment Strategy, alongside limiting investments in only highly rated or UK

Government and other local authorities. As such all investments entered into by the Council in 2010/11 will be deemed to be Specified investments with the exception of any overnight deposits held in the Council's own bank account operated by LloydsTSB which currently falls outside the credit criteria set by the Council.

4.22 Credit rating information is supplied by the Council's treasury consultants. Any counterparty failing to meet the criteria would be omitted from the counterparty list. The Council supplements its credit rating info with additional market information that is applied to compare the relative security of differing investment counterparties – for example Credit Default Swaps.

4.23 The day-to-day decision making on treasury services is supported by the Treasury Management Panel, an officer group that meets regularly to evaluate market information and to review performance and future lending strategies. This Panel is attended by senior officers of the Council and its treasury consultants.

4.24 The security of the Council' investments are also protected using time and monetary limits for institutions on the Council's counterparty list.

4.25 The criteria are clearly laid out in the Investment Strategy and provide a pool of high quality investment counterparties. The counterparty list associated with the 2010/11 Investment Strategy is attached in Annex E.

<u>Treasury Policy Statement</u>

4.26 The over-arching document is the Treasury Policy Statement which recognises the Council's adoption of the Code of Practice. This policy sets out that the Council recognises and achieves the need for;

- Formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of treasury management activities.
- The effective management and control of risk as prime objectives and that responsibility lies clearly within the organisation.
- The pursuit of value for money in treasury management.

4.27 The amended policy is attached in Annex F.

<u>Assessment of Treasury Management</u>

4.28 In line with the Code the Governance and Audit Committee are requested to specifically consider

- The Capital Prudential Indicators and Limits for 2010/11 to 2012/13 contained within Annex A
- The Minimum Revenue Provision Policy contained within Annex B
- The Treasury Management Strategy Statement, and the Treasury Prudential Indicators contained in Annex C
- The Authorised Limit Prudential Indicator contained in Annex C
- The Investment Strategy 2010/11 to 2012/13 and Treasury Management Limits on Activity contained in Annex D
- The Treasury Policy Statement contained in Annex F

Background Papers
CIPFA Code of Practice on Treasury Management in the Public Sector (revised 2009)
CIPFA Prudential Code
Communities and Local Government - Local Authority Investments
Treasury Management report – Council March 2010

Contact for further information
Calvin Orr, Corporate Services – Audit & Technical 01344 352125
calvin.orr@bracknell-forest.gov.uk

Doc. Ref
G:\Technical and Audit\Treasury Management\2010-11 Treasury Management Strategy\Governance and Audit Committee March 2010.doc