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# Audit Committee Agenda

**Thursday, 7 March 2024 at 6.00 pm**

Council Chamber, Muriel Matters House, Breeds Place, Hastings, TN34 3UY. Please enter the building through the Contact Centre entrance via the seafront.

For further information, please contact Democratic Services on 01424 451484 or email: democraticservices@hastings.gov.uk

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| 1. | Apologies for absence | |
| 2. | Declarations of interest | |
| 3. | Minutes of the last meeting | 1 - 6 |
| 4. | Internal Audit Progress Report - Quarter 3 (October 2023 - December 2023)<br>*Mark Winton (Chief Internal Auditor)* | 7 - 18 |
| 5. | Internal Audit Strategy, Internal Audit Plan and Audit Charter 2024/25<br>*Mark Winton (Chief Internal Auditor)* | 19 - 40 |
| 6. | Public Sector Internal Audit Standards (PSIAS) - Self Assessment Summary<br>*Mark Winton (Chief Internal Auditor)* | 41 - 50 |
| 7. | Treasury Management Strategy and Capital Strategy 2024/25<br>*Kit Wheeler (Chief Finance Officer)* | 51 - 118 |
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**AUDIT COMMITTEE**

**7 DECEMBER 2023**

Present: Councillors Foster (Chair), Webb (Vice-Chair), Collins, Marlow-Eastwood and Sinden

In attendance: Kit Wheeler Chief Finance Officer, Mary Kilner Chief Legal Officer, Darren Wells External Auditor (Grant Thornton)

## 6. APOLOGIES FOR ABSENCE

None received.

## 7. DECLARATIONS OF INTEREST

| **Councillor** | **Item** | **Interest** |
|---|---|---|
| Cllr Webb | *All items* | Personal – Is an East Sussex County Councillor, Cabinet member 2021-2022 |
| Cllr Marlow-Eastwood | *All items* | Personal – Is an East Sussex County Councillor |

## 8. MINUTES OF THE LAST MEETING

**RESOLVED – that the minutes of the meeting held on 9th November 2023 be approved as a true record.**

## 9. EXTERNAL AUDITOR'S ANNUAL REPORT ON HASTINGS BOROUGH COUNCIL 2021/22 AND 2022/23

The Chief Finance Officer gave an introduction and highlighted that the report covers two financial years.

The External Auditor presented a report to summarise the principal matters arising because of the audit and assurance work carried out by the Councils External Auditors Grant Thornton. The External Auditor highlighted that for financial sustainability there are significant weaknesses. The finance position is extremely challenging, and the reserves have had to be used. The planned savings for the two financial years was below 100% with 2021-22 being 82% delivered and in 2022-23 78% savings have placed a greater draw on reserves. The second significant weakness is regarding capital investments made. With regards to the Cornwallis Hotel development the External Auditor believes there was not good due diligence completed and that procurement rules were not followed. Regarding Governance the external Auditor highlighted issues in 2021 with internal audit. The improvement from bringing in Orbis should be seen going into 2023-24. It was highlighted that Cabinet review risk at an informal meeting and not a formal meeting and that this is a weakness. There are other elements that are completed at informal meetings, and this makes it unable to be scrutinised or audited. A Key recommendation is that the Council reviews its internal governance arrangements to ensure that business is formalised, and that scrutiny is then able to discharge its responsibilities.

Work is taking place now on the 2020-21 Financial statements. The Government is proposing a backstop and this could happen in March 2024 or September 2024. Because of this the 2021-22 and 2022-23 financial statements are not to be started. The reset would mean that the External Auditor would start in earnest on the 2023-24 financial statements audit and then undertake a programme of work to get assurance on the opening balances for 2023-24.

Twelve recommendations are made in the report. The committee asked questions.

The Chair invited Councillor Patmore (Chair of Overview and Scrutiny) to join the meeting.

Councillor Sinden asked what would happen to the financial statements for 2021-22 and 2023-24? The External Auditor answered this is being assessed and there are no clear answers yet.

Councillor Marlow Eastwood asked regarding Cornwallis Car Park redevelopment and at what level the serious errors were made? The External Auditor explained it was not at a junior level and was Senior Officers and Senior members through Cabinet at the time of the decision making.

Recommendation 1:

Councillor Collins asked regarding the savings and income targets not being met and if the budget targets should be raised? The Chief Finance Officer answered that there are now regular monitoring reports which should highlight where targets are not being achieved and give time to address them. By holding a budget planning meeting in December, it will give the Council a head start to achieve the budget targets.

Councillor Webb asked regarding the direction of travel for the risk identified because of contract procedure breach. The External auditor agreed that the direction of travel is a flat line rather than declining as per the report.

Recommendation 2:

Councillor Patmore asked regarding the delay to the asset management plan and the recommendation to revaluate each asset so that the Councillors understand the risk and rewards. The Chief Finance Officer explained the CIPFA Asset management plan should be ready early in 2024 and that capacity to review every asset would need to be reviewed.

Councillor Collins asked regarding Cornwallis Street redevelopment and if the auditors would have been able to identify the errors earlier? The External Auditor answered that it could have been.

Councillor Sinden asked regarding value for money report for 2023-24. The External Auditor explained that the report in this agenda makes the External Auditor value for money report up to date.

Councillor Patmore asked regarding older investments on retail units and that the Overview and Scrutiny committee have not been able to scrutinize these investments. The Chief Finance Officer explained that previous committees would have scrutinised the decisions made on the investments. Councillor Webb highlighted that it was the officer's advice in 2019 to invest into retail.

Councillor Marlow-Eastwood asked regarding when the Asset management plan will be ready? The Chief Finance Officer explained the report will be ready in the new year. CIPFA have identified some assets that could be bought forward for disposal or change of use.

Councillor Collins asked regarding the Cornwallis Street redevelopment and what role the Chief Executive should have been in terms of oversight of the decision making process. The External Auditor answered that the decision making holistically was not strong enough and the ultimate responsibility does not rest with one officer alone. It rests with the Council as a whole and ultimately through Cabinet as the decision making forum,

The Chair proposed that the Internal Auditors can review ongoing projects as part of their workplan.

Recommendation 3

Councillor Collins asked regarding the Hastings Housing Company and how would the Council get its loans back if it was to fold? The Chief Finance Officer answered that the Hastings Housing company's assets could be sold to repay the debt.

Councillor Marlow-Eastwood asked regarding the summary findings and the strengthening of internal audit. The External Auditor explained that Orbis has a robust approach to risk management and have the resources to complete their work and that the Council using Orbis is a positive.

Councillor Patmore asked regarding more detailed reports and if the level information being given to Councillors is correct. The External Auditor explained the decision-making body should show strength to not make a decision if they don't feel they have been given sufficient information, sufficient depth of information, sufficient analysis or sufficient time.

The Chair asked regarding the Internal Auditors employed by Hasting Borough Council. The Chief Finance Officer answered there are two members of HBC staff who work alongside Orbis and that they solely focus on internal audit.

Recommendation 4

Councillor Sinden asked how to learn from the past events and if there is a survivable future? The External auditor answered the outlook is not promising for local Councils. The Chief Finance Officer explained that several pleas have been made to Government. Regular conversation has been had with the DLUHC to prevent the issuing of a section 114 notice.

Councillor Patmore asked regarding the Hastings Housing Company and how the Council has leant money to itself and now must pursue the money. The Chief Finance Officer explained that when the loan was set up it would have been with the intention of it paying itself and making a profit and there are regulations for PWLB borrowing that were followed.

Councillor Webb highlighted regarding the informal meetings that in 2022 there was a Labour and Green Cabinet. The External Auditor explained that formal meetings give transparency and gives Audit and Overview and Scrutiny an opportunity to review the decisions. Councillor Marlow-Eastwood asked if there are proposals to change the meeting to formal meetings. The External Auditor explained it is not for the External Auditor to explain how this would happen, it would be for officers to propose how that would work and for Councillors to decide. Councillor Patmore asked that Cabinet discussions are more robust.

Recommendation 8:

Councillor Marlow-Eastwood asked if the recommendations have been implemented. The Chief Finance Officer answered that when the recommendations are reviewed next year the recommendations that are agreed with should be implemented.

Recommendation 9:

Councillor Collins asked how to add independent members to the Audit Committee. The Chief Legal Officer answered that this would be passed to the Working Arrangement Group and changes to any the constitution will be reviewed. The External Auditor added it is a CIPFA recommendation to have independent members on the Audit Committee. The Chair proposed to research with other Councils about having independent members. Councillor Marlow-Eastwood highlighted if it is the External Auditors and CIPFA's recommendation then it should be followed.

Recommendation 12:

Councillor Patmore asked about what has been completed to improve the conflicts of interest. The Chief Finance Officer explained procurement has been completely reviewed and aligned with other councils' approach. New guides and training have been given to staff and there are monthly meetings with the procurement hub.

Councillor Marlow Eastwood asked if the Council has a legal position because of conflicts of interest? The Chief Legal Officer answered that training is key and all contracts and commercial transactions will be now reviewed by the legal department.

The plan going forward will be to engage with group leaders in relation to conflicts of interest of Councillors and potential breaches of the code of conduct. Councillor Patmore asked regarding the breach of procurement rules. The Chief Legal Officer explained the transaction happened before her employment with Hastings Borough Council and further due diligence should have been completed.

Follow up of previous recommendations:

Councillor Collins asked that given the scale of the financial sustainability and governance failures which have been outlined, why statutory recommendations report or a public interest report was not submitted. The External Auditor answered that it is felt it would be better to wait for the Council to set its 2024-25 budget as this is seen as a key milestone.

**RESOLVED (unanimously)**
**Agree the recommendations contained in the External Auditors report.**

**Reasons**

To Under Section 20(1)(c) of the Local Government Audit and Accountability Act 2014 the external Auditors have to satisfy themselves that the Council has made proper arrangements for securing economy, efficiency and effectiveness in its use of resources.

## 10. NOTIFICATION OF ANY ADDITIONAL URGENT ITEMS (IF ANY)

None

(The Chair declared the meeting closed at. 7.41 pm)

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| | |
|---|---|
| **Report to:** | **Audit Committee** |
| **Date of Meeting:** | **7 March 2024** |
| **Report Title:** | **Internal Audit Progress Report – Quarter 3 (Oct 2023 – Dec 2023)** |
| **Report By:** | **Mark Winton, Chief Internal Auditor** |

**Purpose of Report**

To provide Members with an update on all internal audit and counter fraud activity completed during the quarter, including a summary of all key findings. To also provide an update on the performance of the internal audit service during the period.

**Recommendation(s)**

**The Committee is recommended to:**

**1. Note the report and consider any further action required in response to the issues raised.**

**Reasons for Recommendations**

i) To comply with the requirements set out in the Public Sector Internal Audit Standards 2013 (amended April 2017).
ii) To support the committees responsibilities for assessing the effectiveness of the internal control environment and the effectiveness of the internal audit service.

## Introduction and Background

This progress report covers work completed between October 2023 and December 2023 against the Indicative Programme of Work, contained within the Internal Audit Strategy approved by this Committee on 17th August 2023.

## Relevant Policy / Professional Standards

1. Internal Audit follows the mandatory standards set out in the Public Sector Internal Audit Standards (PSIAS) published by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors.

# Timetable of Next Steps

2. Please include a list of key actions and the scheduled dates for these:

| Action | Key milestone | Due date (provisional) | Responsible |
|---|---|---|---|
| - | - | - | - |

## Wards Affected

None.

## Implications

Please identify if this report contains any implications for the following:

| | |
|---|---|
| Equalities and Community Cohesiveness | No |
| Crime and Fear of Crime (Section 17) | No |
| Risk Management | Yes |
| Environmental Issues | No |
| Economic/Financial Implications | Yes |
| Human Rights Act | No |
| Organisational Consequences | No |
| Local People's Views | No |
| Anti-Poverty | No |
| Climate Change | No |

## Additional Information

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## Officer to Contact

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Appendix A

# Internal Audit and Counter Fraud

# Quarter 3 Progress Report 2023/24

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## 1. Summary of Completed Audits

1.1 This section provides an update on the audit work completed during the previous quarter.

**Debtors/Accounts Receivable**

1.2 The Accounts Receivable function is responsible for ensuring that all income due to the council is collected effectively, efficiently, and correctly accounted for.

1.3 Between 1st April 2022 and 31st March 2023, 11,044 invoices were raised to a total value of £13.7m, offset by 66 credit notes with a total value of £44,225.

1.4 This audit sought to provide assurance over the key controls operating within the Accounts Receivable system, including those in place for ensuring the accuracy of customer details, the timeliness and accuracy of invoicing, the recording and matching of payments to invoices and the overall completeness of debt recovery.

1.5 The audit did not review the collection of Council Tax Reduction Scheme overpayments which may be part of a separate audit in the future.

1.6 Based on the work undertaken, we were able to provide an opinion of **Partial Assurance** over the controls operating for the following reasons:

1.7 There is no comprehensive debt management policy currently in place which details how, when, and in what circumstances staff should raise invoices, leading to inconsistencies and delays in the debt recovery process. Roles and responsibilities concerning the approval of sales orders are not clearly defined. Consequently, sales orders are generally approved without sight of supporting evidence (e.g. proof of debt). In such circumstances, there is a risk that sales orders could be raised inaccurately, requiring significant resources to be rectified and potential for future recovery action to be compromised, especially if evidence has been lost or invoices have been created in error.

1.8 Reconciliations between the Debtors Control account and the General Ledger have not been completed in the last two and a half years. As such, there is a risk that posting errors have not been identified, leading to errors in the financial statements.

1.9 No time is allocated to debt recovery exercises such as targeting cases profiled by age, value or type and, other than Aged Debt and Cost Centre reports, no useful reports exist to provide key performance information.

1.10 At present, no procedure exists detailing how and when debts should be referred to Legal Services or be written off. No invoices have been written off in over twelve months and large volumes of cases remain on hold, pending write-off or referral to Legal Services. As such, there is a significant risk that debts owed to the council have not been pursued through legal action or otherwise followed up.

1.11 The Accounts Receivable Team have developed efficient processes for reviewing requests for new customer accounts and raising invoices. This means that sales orders are either rejected or converted to invoices and emailed to customers in a timely fashion. This audit was able to obtain sufficient evidence from the Service Teams to support general debt recovery actions taken but as detailed above, this evidence was not contained within the finance system.

1.12 Instructions supporting the raising of invoices and a robust process for matching payments to invoices and resolving customer payment errors has been developed. An innovative way to return erroneous payments or part payment to the customer via the bank has also been developed, which was found to be subject to appropriate authorisations and separation of duties and means that a Debtors Suspense account is not required.

1.13 The Council recently started work to attempt to deal with the increasing risk associated with debt recovery. A Debt Recovery Working Group has been established to pro-actively look at all aspects of debt management across the Council and a Debt Management Policy is under development as part of this work.

1.14 Fourteen medium risk actions and one low risk action have been agreed with management to improve the control environment and these will feed into the Debt Recovery Working Group where appropriate. All high risk agreed actions will be subject to action tracking and we will undertake a follow-up audit in the next financial year to assess the extent of progress made.

**Business Continuity**

1.15 The Civil Contingencies Act 2004 places a statutory duty on local authorities, as a category one responder, to develop, maintain and test Business Continuity Plans (BCPs).

1.16 Effective business continuity planning helps to provide a controlled resumption of prioritised services within expected timescales, ensures an organisation can deliver a satisfactory, pre-defined, level of business operations in response to a disruption to business as usual.

1.17 Business continuity policies and plans for individual services were produced in 2018 and due for review in 2021, however, the onset of Covid-19 delayed this work. The additional responsibilities and pressures experienced by staff at that time have meant that these plans are only now in the progress of being fully reviewed.

1.18 The objective of this review was to advise on the controls that should be in place to manage key risks to the achievement of service objectives for business continuity. As such, this was a light touch piece of work aimed at providing timely input to the process to improve business continuity arrangements so no formal audit opinion was provided.

1.19 We did not review the current operating arrangements with East Sussex County Council in terms of the supply of a part time Emergency Planning Officer under the East Sussex Resilience and Emergencies Partnership (ESREP) as this was outside of the scope.

1.20 Following a recent management restructure, the Head of Community and Regulatory Services has now taken over responsibility for the Hastings Borough Council Business Continuity Policy and Framework and has begun the programme of addressing business continuity arrangements for the council.

1.21 Plans are in the early stages of being reviewed with more work required to bring policies and procedures up to date. In addition, work is required to set up a Business Continuity Board to review incidents, provide oversight and ensure best practice. It is already evident that good progress is being made.

1.22 This will require a commitment from all services, including Senior Leadership Team to bring business continuity up to operational readiness.

1.23 The Council is working in partnership with East Sussex County Council to share best practice and develop effective business continuity arrangements, utilising the expertise of the Emergency Planning Officer through the ESREP partnership.

1.24 We agreed actions in relation to nine medium risk findings which will support improvements to the control environment. A full audit is planned, potentially in 2025/26, to review the business continuity arrangements once they have been fully embedded.

**Support to the Debt Recovery Project**

1.25 Internal Audit continue to provide independent advice to the Council's Debt Recovery Project. This included a report identifying a number of areas for the project to consider.

## 2. Counter Fraud and Investigation Activities

2.1 No specific counter fraud activity has been required or conducted in the reporting period.

## 3. Action Tracking

3.1 Internal Audit will continue to work with senior management to ensure that sufficient attention is given to any high priority actions that are overdue, and an update on progress with high priority actions will continue to be reported to this committee.

## 4. Amendments to the Indicative Programme of Work

4.1 In accordance with proper professional practice, the Internal Audit indicative programme of work for the year is kept under regular review to ensure that the service continues to focus its resources in the highest priority areas based on an assessment of risk. Through discussions with management, no further amendments have been made to the indicative programme at this stage.

4.2 Members are reminded that the focus for the 2023/24 financial year remains on service development and as such, we do not expect all audits from the indicative programme of work to be completed in full. However, we are making good progress against the programme with all the remaining assignments in progress (Cyber Security and Organisational Resilience, Risk Management, Payroll and the certification of the Home Upgrade Phase 2 Grant). We will provide further updates to Audit Committee over the course of the year.

## 5. Service Development Plan

5.1 During Quarter 3 the team have been focused on embedding our approach to undertaking robust and effective internal audit work and developing relationships with key stakeholders.

5.2 A self-assessment against the Public Sector Internal Audit Standards is due to be completed in February 2024 and the results will be reported to the Audit Committee alongside the next Internal Audit progress report.

5.3 The annual audit plan is also in development for the 2024/25 financial year.

## 6. Internal Audit Performance

6.1 It is a key responsibility of the Audit Committee to satisfy itself as to the ongoing effectiveness of the Council's internal audit arrangements, with the service's conformance against Public Sector Internal Audit Standards key to forming this judgement. Such conformance is self-assessed by the service annually and independently externally assessed at least every five years, all of which is reported to the Audit Committee. In addition to this, performance against a range of key performance indicators is measured on a quarterly basis, with the results reported to the committee throughout the year.

6.2 It is, however, important to note that the service at HBC has not in our view, been historically conforming with professional standards and requires significant improvement, all of which is being addressed, as explained above. Furthermore, key performance indicators have not previously been in place for the service and are only now being introduced for the first time. Given this situation, it is not currently possible to report in full against these measures, with more complete reporting due to be implemented for 2024/25. In meantime, we have set out below the agreed key performance measures for the service, with some results included where these are available:

| Aspect of Service | Orbis IA KPI | Target | RAG Score | Actual Performance |
|---|---|---|---|---|
| **Quality** | Annual Audit Plan agreed by Audit Committee | By end April | G | Indicative programme of work approved by the Audit Committee on 17th August 2023. |
| | Annual Audit Report and Opinion | By end July | N/A | Annual Audit Report and Opinion not yet due. |
| | Customer Satisfaction levels | 90% satisfied | G | 100% |
| **Productivity and process efficiency** | Audit Plan – completion to draft report stage | 90% | N/A | Indicative programme of work only in place for current year, with focus on service improvement. |

| | | | | |
|---|---|---|---|---|
| **Compliance with professional standards** | Public Sector Internal Audit Standards complied with | Conforms | **N/A** | Self-assessment against PSIAS will be undertaken in February 2024. |
| | Relevant legislation such as the Police and Criminal Evidence Act, Criminal Procedures and Investigations Act | Conforms | **G** | No evidence of non-compliance identified. |
| **Outcome and degree of influence** | Implementation of management actions agreed in response to audit findings | 95% for high priority agreed actions | **N/A** | All future high priority actions will be subject to action tracking. |
| **Our staff** | Professionally qualified / accredited | 80% | **G** | 100% including part qualified. |

Appendix B

# Audit Opinions and Definitions

| Opinion | Definition |
|---|---|
| **Substantial Assurance** | Controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives. |
| **Reasonable Assurance** | Most controls are in place and are operating as expected to manage key risks to the achievement of system or service objectives. |
| **Partial Assurance** | There are weaknesses in the system of control and/or the level of non-compliance is such as to put the achievement of the system or service objectives at risk. |
| **Minimal Assurance** | Controls are generally weak or non-existent, leaving the system open to the risk of significant error or fraud. There is a high risk to the ability of the system/service to meet its objectives. |

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|---|---|
| **Report to:** | **Audit Committee** |
| **Date of Meeting:** | **7 March 2024** |
| **Report Title:** | **Internal Audit Strategy, Internal Audit Plan and Audit Charter 2024/25** |
| **Report By:** | **Mark Winton, Chief Internal Auditor** |

## Purpose of Report

To present to the Audit Committee the Council's Internal Audit Strategy and Internal Audit Plan for 2024/25.

## Recommendation(s)

**The Committee is recommended to:**

**1. Approve the Council's Internal Audit Strategy, Internal Audit Plan and Audit Charter for 2024/25.**

## Reasons for Recommendations

i) To comply with the requirements set out in the Public Sector Internal Audit Standards 2013 (amended April 2017).

ii) The Audit Committee is responsible for reviewing the effectiveness of the Council's system of internal control.

## Introduction and Background

1. The Council's Internal Audit Strategy and Internal Audit Plan 2024/25 (Annexe A) set out how the Council will meet its statutory requirements for internal audit, as defined within the Accounts and Audit Regulations 2015.

### Relevant Policy / Professional Standards

2. Internal Audit follows the mandatory standards set out in the Public Sector Internal Audit Standards (PSIAS) published by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors.

3. The Annual Audit Plan 2024/25 allows sufficient coverage to form an overall opinion, with time to continue to develop the service to meet the expectations of these Standards.

## Timetable of Next Steps

4. Please include a list of key actions and the scheduled dates for these:

| Action | Key milestone | Due date (provisional) | Responsible |
|---|---|---|---|
| - | - | - | - |

### Wards Affected

None.

### Implications

Please identify if this report contains any implications for the following:

| | |
|---|---|
| Equalities and Community Cohesiveness | No |
| Crime and Fear of Crime (Section 17) | No |
| Risk Management | Yes |
| Environmental Issues | No |
| Economic/Financial Implications | Yes |
| Human Rights Act | No |
| Organisational Consequences | No |
| Local People's Views | No |

| | |
|---|---|
| Anti-Poverty | No |
| Climate Change | No |

**Additional Information**

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**Officer to Contact**

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# Internal Audit Strategy and Internal Audit Plan 2024-25

## 1. Role of Internal Audit

1.1 The full role and scope of the Council's Internal Audit Service is set out within the Internal Audit Charter and Terms of Reference (attached as Appendix B).

1.2 The mission of Internal Audit, as defined by the Chartered Institute of Internal Auditors (CIIA), is to enhance and protect organisational value by providing risk-based and objective assurance, advice and insight. Internal Audit is defined as "an independent, objective assurance and consulting activity designed to add value and improve an organisation's operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control and governance processes."

1.3 The organisation's response to internal audit activity should lead to a strengthening of the control environment, thus contributing to the overall achievement of organisational objectives.

## 2. Risk Assessment and Audit Planning

2.1 Cabinet agreed to Orbis Internal Audit providing resource to fulfil the role of Chief Internal Auditor and to support improvements to the Internal Audit service for 2023/24. An indicative programme of work was agreed with Audit Committee for this initial year.

2.2 In January 2024, Hastings Brough Council (HBC) Cabinet agreed to Orbis IA providing the internal audit service to HBC for the next five years and it is following this decision that we are able to present an annual audit plan for 2024/25.

2.3 HBC's Internal Audit Strategy and Annual Audit Plan is updated annually and is based on a number of factors, especially management's assessment of risk (including that set out within the strategic and departmental risk registers) and our own risk assessment of the Council's major systems and other auditable areas. This allows us to prioritise those areas to be included within the audit plan on the basis of risk.

2.4 The annual planning process has involved consultation with a range of stakeholders to ensure that their views on risks and current issues, within individual departments and corporately, are identified and considered. In order to ensure that the most effective use is made of available resources, to avoid duplication and to minimise service disruption, efforts will continue to be made to identify, and where possible, rely upon, other sources of assurance available. The following diagram sets out the various sources of information used to inform our 2024/25 audit planning process:


2.5 Through this process, we have been able to identify key areas for audit activity in 2024/25, including strategic risks and issues, key priority projects and programmes, priority service reviews, key financial systems, and grant claims. The remainder of the direct audit days are earmarked as emerging risks/contingency which enables us to respond to the rapidly changing risk landscape across the Authority.

2.6 In producing the audit plan (which is set out in Appendix A to this report) the following key principles will be applied:

- Key financial systems are subject to a cyclical programme of audits covering, as a minimum, compliance against key controls;
- Previous reviews which resulted in either 'minimal' or 'partial' assurance audit opinions will be subject to a specific follow-up review to assess the effective implementation by management of agreed actions.

2.7 The 2024/25 audit plan remains flexible. This is in part due to the potential impact any move to shared services working may have on our ability to deliver the audit plan, and also because the changing nature of the risk landscape across the public sector. Given the likelihood of the plan needing to flex within the year ahead, we have identified a number of additional audit assignments that may, on a risk-prioritised basis, be drawn into our workload if planned audits are postponed or cancelled.

2.8 In addition, formal action tracking arrangements have been introduced to monitor the implementation by management of all individual high risk agreed actions. The results of action tracking on high risk agreed actions will be reported to the Audit Committee on a quarterly basis.

2.6 Since 2018, Surrey County Council, East Sussex County Council and Brighton and Hove City Council have been working together to establish and develop the Orbis Internal Audit Partnership. In doing, we are able to deliver high quality and cost effective assurance services to all of our partner and client councils, drawing upon the wide range of skills and experience from across the various teams. The size and scale of the partnership has also enabled us to invest in specialist IT Audit and Counter Fraud services, to the benefit of all clients.

## 3. Key Issues

2.9 The internal audit plan does not seek to provide assurance over all high and emerging risks currently faced by the Council. Instead, its aim is to provide assurance over some of the Council's core functions and activities, whilst also allowing new working practices within the Internal Audit to continue to be established.

3.2 In times of significant transformation, organisations must both manage change effectively and ensure that core controls remain in place. In order to respond to the continued reduction in financial resources and the increased demand for services, the Council needs to consider some radical changes to its service offer in many areas.

3.3 Internal Audit must therefore be in a position to give an opinion and assurance that covers the control environment in relation to both existing systems and these new developments. It is also essential that this work is undertaken in a flexible and supportive manner, in conjunction with management, to ensure that both risks and opportunities are properly considered. During 2024/25, a number of major organisational initiatives and/or risks will feature within the audit plan, with the intention that Internal Audit is able to provide proactive advice, support and assurance as these programmes progress. These include:

- Council's Debt Recovery Project.
- Temporary Accommodation;
- Shared Services Programme Governance and Risk Management Arrangements.

3.4 In recognition that in some cases, sufficient information regarding the full extent of future changes and associated risks may not yet be known, the 2024/25 audit plan includes a proportion of time classified as 'Emerging Risks'. This approach has been adopted to enable Internal Audit to react appropriately throughout the year as new risks materialise and to ensure that expertise in governance, risk and internal control can be utilised early in the change process.

3.5 In view of the above, Internal Audit will continue to work closely with senior management and Members throughout the year to identify any new risks and to agree how and where audit resources can be utilised to best effect.

3.6 Other priority areas identified for inclusion within the audit plan include:
- Key Financial Systems
- Corporate Governance
- Organisational Resilience
- Contract Management
- Unit 4 - Upgrade Management

3.7 The results of all audit work undertaken will be summarised within quarterly update reports to the Senior Leadership Team, and the Audit Committee, along with any common themes and findings arising from our work.

## 4. Counter Fraud

4.1 Managing the risk of fraud and corruption is the responsibility of management. Internal Audit will, however, be alert in all its work to risks and exposures that could allow fraud or corruption.

4.2 The Chief Internal Auditor should be informed of all suspected or detected fraud, corruption or irregularity in order to consider the adequacy of the relevant controls and evaluate the implication for their opinion on the control environment.

4.3 In addition, Internal Audit will support promotion of an anti-fraud and corruption culture within the Council to aid the prevention and detection of fraud. In 2024/25, through the work of the Counter Fraud Team, Internal Audit will undertake a fraud risk assessment and develop a programme of proactive and reactive counter fraud services to help ensure that the Council continues to protect its services from fraud loss.

## 5. Matching Audit Needs to Resources

5.1 The overall aim of the Internal Audit Strategy is to allocate available internal audit resources so as to focus on the highest risk areas and to enable an annual opinion to be given on the adequacy and effectiveness of the Council's governance, risk and control framework.

5.2 Orbis Internal Audit is contracted to provide 400 days to Hastings Borough Council for the provision of internal audit and counter fraud services.

5.3 At the time of the producing this plan, arrangements are in place to TUPE transfer staff from HBC into East Sussex County Council (as host for Orbis). Once completed, internal audit activities will be delivered by a range of staff from across the Orbis Internal Audit Service, maximising the value from a wide range of skills and experience available. In the small number of instances where sufficient expertise is not available from within the team, mainly in highly technical areas, externally provided specialist resources may be utilised.

## 6. Audit Approach

6.1 The approach of Internal Audit is to use risk based reviews, supplemented in some areas by the use of compliance audits and themed reviews. All audits have regard to management's arrangements for:

- Achievement of the organisation's objectives;
- Reliability and integrity of financial and operational information;
- Effectiveness and efficiency of operations and programmes;
- Safeguarding of assets; and
- Compliance with laws, regulations, policies, procedures and contracts.

6.2 In addition to these audits, and the advice on controls given on specific development areas which are separately identified within the indicative programme of work, there are a number of generic areas where there are increasing demands upon Internal Audit, some of which cannot be planned in advance. For this reason, time is built into the indicative programme of work to cover the following:

- Contingency – an allowance of days to provide capacity for unplanned work, including special audits and management investigations;

- Advice, Management, Liaison and Planning - an allowance to cover provision of ad hoc advice on risk, audit and control issues, audit planning and annual reporting, ongoing liaison with service management and Members, and audit management time in support of the delivery of all audit work, planned and unplanned.

- Service Development – An allowance to support the development of the service to improve overall levels of compliance with the Public Sector Internal Audit Standards (PSIAS).

6.3 In delivering this strategy and indicative programme of work, we will ensure that liaison takes place with the Council's external auditors, to ensure that the use of audit resources is maximised, duplication of work is avoided, and statutory requirements are met.

## 7. Training and Development

7.1 The effectiveness of the Internal Audit Service depends significantly on the quality, training and experience of its staff. Training needs of individual staff members will be identified through a formal performance and development process and are delivered and monitored through on-going management supervision.

7.2 The team is also committed to coaching and mentoring its staff, and to providing opportunities for appropriate professional development. This is reflected in the high proportion of staff holding a professional internal audit or accountancy qualification as well as numerous members of the team continuing with professional training during 2024/25.

## 8. Quality and Performance

8.1 With effect from 1 April 2013, all of the relevant internal audit standard setting bodies, including CIPFA, adopted a common set of Public Sector Internal Audit Standards (PSIAS). These are based on the Institute of Internal Auditors International Professional Practices Framework and replace the previous Code of Practice for Internal Audit in Local Government.

8.2 Included within the new Standards is the requirement for the organisation to define the terms 'Board' and 'senior management' in the context of audit activity. This has been set out within the Internal Audit Charter, which confirms the Audit Committee's role as the Board.

8.3 The PSIAS require each internal audit service to maintain an ongoing quality assurance and improvement programme based on an annual self-assessment against the Standards, supplemented at least every five years by a full independent external assessment. The outcomes from these assessments, including any improvement actions arising, will be reported to the Audit Committee, usually as part of the annual internal audit report. For clarity, the Standards specify that the following core principles underpin an effective internal audit service:

- Demonstrates integrity;

- Demonstrates competence and due professional care;
- Is objective and free from undue influence (independent);
- Aligns with the strategies, objectives, and risks of the organisation;
- Is appropriately positioned and adequately resourced;
- Demonstrates quality and continuous improvement;
- Communicates effectively;
- Provides risk-based assurance;
- Is insightful, proactive, and future-focused;
- Promotes organisational improvement.

8.4 In addition, the performance of Internal Audit continues to be measured against key service targets focussing on service quality, productivity and efficiency, compliance with professional standards, influence and our staff. These are all underpinned by appropriate key performance indicators as set out in Table 2 below.

8.5 At a detailed level each audit assignment is monitored and customer feedback sought. There is also ongoing performance and development reviews and supervision for all Internal Audit staff during the year to support them in achieving their personal targets.

8.6 In addition to the individual reports to management for each audit assignment, reports on key audit findings and the delivery of the indicative programme of work are made to the Audit Committee on a quarterly basis. An Annual Internal Audit Opinion is also produced each year.

8.7 Whilst Orbis Internal Audit liaises closely with other internal audit services through the Sussex and Surrey audit and counter fraud groups, the Home Counties Chief Internal Auditors' Group and the Local Authority Chief Auditors' Network, we are continuing to develop joint working arrangements with other local authority audit teams to help improve resilience and make better use of our collective resources.

***Table 2*: Performance Indicators**

| Aspect of Service | Orbis IA Performance Indicators | Target |
|---|---|---|
| **Quality** | • Annual Audit Plan agreed by Audit Committee (2024/25)<br>• Annual Audit Report and Opinion (2023/24)<br>• Satisfaction levels | By end March 2024<br>To inform AGS by June 2024<br>90% satisfied |
| **Productivity and Process Efficiency** | • Audit Plan – completion to draft report stage by 31 March 2024 | 90% |
| **Compliance with Professional Standards** | • Public Sector Internal Audit Standards<br>• Relevant legislation such as the Police and Criminal Evidence Act, Criminal Procedures and Investigations Act | Conforms<br>Conforms |

| | | |
|---|---|---|
| | | |
| **Outcomes and degree of influence** | • Implementation of management actions agreed in response to audit findings | 95% for high priority actions |
| **Our Staff** | • Professionally Qualified/Accredited | 80% |

Mark Winton
Hastings Borough Council - Chief Internal Auditor
March 2024

# Internal Audit Plan
# 2024-25

Hastings.gov.uk Borough Council

**Planned Audit Reviews**

| **Review Name** | **Outline Objective** |
|---|---|
| **<u>Key Financial Systems</u>** | |
| Treasury Management | To review the adequacy of key controls and procedures across the Council's treasury management arrangements, including cash flow forecasting, segregation of duties, financial investments and use of treasury advisers. |
| Council Tax | To provide assurance that controls over Council Tax collection are effective, including billing, collection, recovery, and the award of discounts. |
| Creditors (Accounts Payable) | To review the processes and key controls relating to the Accounts Payable system, including those in place for ensuring the accuracy of vendor details, the processing of invoices, goods receipting and promptness of payments. |
| Corporate Credit Cards | To evaluate the effectiveness of the controls operating to ensure that spending on the corporate credit cards is appropriate, justified and reasonable. |
| Debtors (Accounts Receivable) - Follow-Up | To review and assess the implementation of the agreed actions arising from the Debtors audit that was completed in 2023/24 which received an audit opinion of partial assurance. |
| **<u>Key Governance Arrangements</u>** | |
| Organisational Resilience (Impact of savings plans) | This review will seek to provide assurance that savings proposals are subject to appropriate challenge and scrutiny and that robust monitoring arrangements are in place to support their implementation. We will also evaluate whether the potential impact of planned savings is sufficiently understood to allow balanced decision-making that manages risks to the Council's strategic objectives effectively, including the delivery of its statutory services. |
| Shared Services Programme Governance and Risk Management Arrangements | To review the programme governance and risk management controls in place for the Shared Services Programme. |
| Corporate Governance | To review the Code of Corporate Governance (including associated policies such as the Code of Conduct, Gifts and Hospitality etc) to provide an opinion on the effectiveness of overall governance arrangements of the Council. |

# Internal Audit Plan 2024-25

Hastings.gov.uk Borough Council

| Review Name | Outline Objective |
|---|---|
| **Strategic Risks/Projects** | |
| Contract Management | The purpose of this audit is to assess the adequacy and effectiveness of contract management arrangements within the Council, specifically in relation to reviewing the adequacy of the contract management framework, guidance, and training for relevant officers and the extent to which this is being complied with across the Authority. |
| Temporary Accommodation | A review of the Council's temporary accommodation arrangements, including the controls to manage financial management risks. |
| **IT Audits** | |
| Unit 4 - Upgrade Management | A review to seek assurance that all future upgrades and updates to the Council's Enterprise Resource Planning (ERP) are appropriately managed to ensure that the system continues to function as expected. |

## Internal Audit Service Management and Delivery

| Review Name | Outline Objective |
|---|---|
| Action Tracking | Ongoing action tracking and reporting of high priority actions. |
| Annual Internal Audit Report and Opinion | Creation of Annual Report and Opinion. |
| Audit and Fraud Management | Overall management of all audit and service development activity, including work allocation, work scheduling. |
| Audit and Fraud Reporting | Production of periodic reports to the Senior Leadership Team and the Audit Committee covering the results of all audit and anti-fraud activity. |
| Audit Committee and other Member Support | Ongoing liaison with Members on internal audit matters and attending Audit Committee meetings and associated pre-meetings as appropriate. |
| Client Service Liaison | Liaison with clients and departmental management teams throughout the year. |
| Client Support and Advice | Ad hoc advice, guidance and support on risk, internal control and governance matters provided to clients and services throughout the year. |

| | |
|---|---|
| **Internal Audit Plan 2024-25** | |

| | |
|---|---|
| External Liaison | Liaison with external auditors and other external bodies, including attendance at regional and national audit groups and counter fraud hubs. |
| Organisational Management Support | Corporate Governance Group; Risk Management; and Management meetings (e.g. Departmental Team Meetings; Manager's Forums; Conferences). |
| Strategy and Annual Audit Planning | Development and production of the Internal Audit Strategy and Annual Audit Plan, including consultation with management and Members. |

| |
|---|
| **Other Auditable Areas Identified During the Audit Planning Process** |
| A number of reviews may be brought forward into the plan if there is additional capacity during the year. In addition, we will consider any emerging risks and prioritise audits accordingly. |

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# HASTINGS BOROUGH COUNCIL
# Audit Charter

## 1. Introduction

This Charter describes for the Council the purpose, authority, and responsibilities of the Internal Audit function in accordance with the UK Public Sector Internal Audit Standards (PSIAS).

The PSIAS require that the Charter must be reviewed periodically and presented to “senior management” and “the board” for approval. For the purposes of this charter “senior management” will be the Senior Leadership Team (SLT) and the “board” will be the Audit Committee.

The Charter shall be reviewed annually and approved by SLT and the Audit Committee. The Chief Internal Auditor is responsible for applying this Charter and keeping it up to date.

## 2. Internal Audit Purpose

The mission of Internal Audit is to enhance and protect organisational value by providing risk-based and objective assurance, advice, and insight.

Internal Audit is defined in the PSIAS as “an independent, objective assurance and consulting activity designed to add value and improve an organisation’s operations. It helps an organisation accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes.”

Internal Audit supports the whole Council to deliver economic, efficient, and effective services and achieve the Council’s vision, priorities and values.

## 3. Statutory Requirement

Internal Audit is a statutory service in the context of the Accounts and Audit Regulations 2015, which require every local authority to maintain an effective internal audit to evaluate the effectiveness of its risk management, control and governance processes taking into account public sector internal auditing standards or guidance.

These regulations require any officer or Member of the Council to
- make available such documents and records; and
- supply such information and explanations;

as are considered necessary by those conducting the audit.

This statutory role is recognised and endorsed within the Council’s Constitution.

In addition, the Council's S151 Officer has a statutory duty under Section 151 of the Local Government Act 1972 to establish a clear framework for the proper administration of the authority's financial affairs. To perform that duty the Section 151 Officer relies, amongst other things, upon the work of Internal Audit in reviewing the operation of systems of internal control and financial management.

## 4. Internal Audit Responsibilities and Scope

Annually the Chief Internal Auditor is required to provide to the Audit Committee an overall opinion on the Council’s internal control environment, risk management arrangements and governance framework to support the Annual Governance Statement.

Internal Audit is not responsible for control systems. Responsibility for effective internal control and risk management rests with the management of the Council.

Internal Audit activity must be free from interference in determining the scope of activity, performing work, and communicating results.

The scope of Internal Audit includes the entire control environment and therefore all of the Council’s operations, resources, services and responsibilities in relation to other bodies. In order to identify audit coverage, activities are prioritised based on risk, using a combination of Internal Audit and management risk assessment (as set out within Council risk registers). Extensive consultation also takes place with key stakeholders and horizon scanning is undertaken to ensure audit activity is proactive and future focussed.

Internal audit activity will include an evaluation of the effectiveness of the organisation’s risk management arrangements and risk exposures relating to:

- Achievement of the organisation’s strategic objectives;
- Reliability and integrity of financial and operational information;
- Efficiency and effectiveness of operations and activities;
- Safeguarding of assets; and
- Compliance with laws, regulations, policies, procedures, and contracts

## 5. Independence

Internal Audit will remain sufficiently independent of the activities that it audits to enable auditors to perform their duties in a way that allows them to make impartial and effective professional judgements and recommendations. Internal auditors should have no operational responsibilities.

Internal Audit is involved in the determination of its priorities in consultation with those charged with governance. The Chief Internal Auditor has direct access to, and freedom to report in their own name and without fear of favour to, all officers and Members and particularly those charged with governance. This independence is further safeguarded by ensuring that the Chief Internal Auditor's formal appraisal/performance review is not inappropriately influenced by those subject to audit.

All Internal Audit staff are required to make an annual declaration of interest to ensure that objectivity is not impaired and that any potential conflicts of interest are appropriately managed.

## 6. Reporting Lines

The Chief Internal Auditor reports to the Chief Finance Officer (S151 Officer) although regardless of line management arrangements, the Chief Internal Auditor has free and unfettered access to report to the Monitoring Officer; the Chief Executive; SLT; the Audit Committee Chair; the Leader of the Council and the Council's External Auditor.

The Audit Committee will receive reports on a periodic basis on the results of audit activity and details of Internal Audit performance including progress on delivering the audit plan.

## 7. Fraud & Corruption

Managing the risk of fraud and corruption is the responsibility of management. Internal Audit will however be alert in all its work to risks and exposures that could allow fraud or corruption and will investigate allegations of fraud and corruption in line with the Council's Counter Fraud and Corruption Strategy and Framework.

The Chief Internal Auditor should be informed of all suspected or detected fraud, corruption, or irregularity in order to consider the adequacy of the relevant controls and evaluate the implication for their opinion on the control environment.

Internal Audit will promote an anti-fraud and corruption culture within the Council to aid the prevention and detection of fraud.

## 8. Consultancy Work

Internal Audit may also provide consultancy services, generally advisory in nature, at the request of the organisation. In such circumstances, appropriate arrangements will be put in place to safeguard the independence of Internal Audit and, where this work is not already included within the approved audit plan and may affect the level of assurance work undertaken, this will be reported to the Audit Committee.

To help services to develop greater understanding of audit work and have a point of contact in relation to any support they may need, Internal Audit will periodically with management discuss emerging risks and key developments within services that may impact on its work.

## 9. Resources

The work of Internal Audit is driven by the annual Internal Audit, which is approved each year by the Audit Committee. The Chief Internal Auditor is responsible for ensuring that Internal Audit resources are sufficient to meet its responsibilities and achieve its objectives.

Internal Audit must be appropriately staffed in terms of numbers, grades, qualifications and experience, having regard to its objectives and to professional standards. Internal Auditors need to be properly trained to fulfil their responsibilities and should maintain their professional competence through an appropriate ongoing development programme.

The Chief Internal Auditor is responsible for appointing Internal Audit staff and will ensure that appointments are made in order to achieve the appropriate mix of qualifications, experience and audit skills. The Chief Internal Auditor may engage the use of external resources where it is considered appropriate, including the use of specialist providers.

## 10. Due Professional Care

The work of Internal Audit will be performed with due professional care and in accordance with the UK Public Sector Internal Audit Standards (PSIAS), the Accounts and Audit Regulations (2015) and with any other relevant statutory obligations and regulations.

In carrying out their work, Internal Auditors must exercise due professional care by considering:

(i) The extent of work needed to achieve the required objectives;

(ii) The relative complexity, materiality or significance of matters to which assurance procedures should be applied; and

(iii) The adequacy and effectiveness of governance, risk management and control processes;

(iv) The probability of significant errors, fraud or non-compliance; and

(v) The cost of assurance in proportion to the potential benefits.

Internal Auditors will also have due regard to the Seven Principles of Public Life – Selflessness; Integrity, Objectivity; Accountability; Openness; Honesty; and Leadership.

## 11. Quality Assurance

The Chief Internal Auditor will control the work of Internal Audit at each level of operation to ensure that a continuously effective level of performance – compliant with the PSIAS is maintained.

A Quality Assurance Improvement Programme (QAIP) is being put in place which is designed to provide reasonable assurance to its key stakeholders that Internal Audit:

- Performs its work in accordance with its charter;
- Operates in an effective and efficient manner; and,
- Is adding value and continually improving the service that it provides.

The QAIP requires an annual review of the effectiveness of the system of Internal Audit to be conducted. Instances of non-conformance with the PSIAS, including the impact of any such non-conformance, must be disclosed to the Audit Committee. Any significant deviations must be considered for inclusion in the Council's Annual Governance Statement.

March 2024

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# Agenda Item 6

**Report to:** **Audit Committee**

**Date of Meeting:** **7 March 2024**

**Report Title:** **Public Sector Internal Audit Standards (PSIAS) – Self Assessment Summary**

**Report By:** **Mark Winton, Chief Internal Auditor**

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**Purpose of Report**

This report provides Members with an update on the outcome of the Self-Assessment against the Public Sector Internal Audit Standards (PSIAS).

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**Recommendation(s)**

**The Committee is recommended to:**

**1. Note the report and the next steps in achieving further the level of compliance.**

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**Reasons for Recommendations**

i) To comply with the requirements set out in the Public Sector Internal Audit Standards 2013 (amended April 2017).

ii) To support the committees responsibilities for assessing the effectiveness of the internal control environment and the effectiveness of the internal audit service.

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## Introduction and Background

As previously agreed with Audit Committee Members, a self-assessment against the Public Sector Internal Audit Standards (PSIAS) was undertaken in February 2024.

This report provides Members with an update on the outcome of the Self-Assessment. The report summarises the results of the Self-Assessment, details the areas of non and partial compliance and identifies the next steps in achieving compliance (where appropriate).

### Relevant Policy / Professional Standards

1. Internal Audit follows the mandatory standards set out in the Public Sector Internal Audit Standards (PSIAS) published by the Chartered Institute of Public Finance and Accountancy (CIPFA) and the Chartered Institute of Internal Auditors.

## Timetable of Next Steps

2. Please include a list of key actions and the scheduled dates for these:

| Action | Key milestone | Due date (provisional) | Responsible |
|---|---|---|---|
| - | - | - | - |

### Wards Affected

None.

### Implications

Please identify if this report contains any implications for the following:

| | |
|---|---|
| Equalities and Community Cohesiveness | No |
| Crime and Fear of Crime (Section 17) | No |
| Risk Management | Yes |
| Environmental Issues | No |
| Economic/Financial Implications | Yes |
| Human Rights Act | No |
| Organisational Consequences | No |
| Local People's Views | No |
| Anti-Poverty | No |
| Climate Change | No |

## Additional Information

-

## Officer to Contact

Mark Winton, Chief Internal Auditor
Email: mark.winton@eastsussex.gov.uk

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# Public Sector Internal Audit Standards – Self Assessment – Summary Report

# February 2024

## 1. Introduction

1.1 Introduced in 2013 and updated in 2017, Public Sector Internal Audit Standards (PSIAS) define the nature of internal audit across the UK public sector. They set principles and a framework for internal audit services to deliver in order to provide a professional service and establish the basis for the evaluation of internal audit performance.

1.2 The PSIAS requires an annual self-assessment and independent external assessment every five years.

1.3 This report summarises the results of the self-assessment, details the areas of non and partial compliance and identifies the next steps in achieving compliance (where appropriate).

1.4 The PSIAS apply to all internal audit service providers, whether in-house, shared services or outsourced.

1.5 The PSIAS assess 2 areas:

- **the Attribute Standards**, which look at the characteristics of the organisation and the individuals performing internal audits.
- **the Performance Standards**, which describe the nature of internal auditing and provide quality criteria against which the performance of these services can be measured.

1.6 The Attribute Standards cover the following areas:

- Purpose, Authority, and Responsibility;
- Independence and Objectivity;
- Proficiency and Due Professional Care; and
- Quality Assurance and Improvement Program.

1.7 The Performance Standards cover the following areas:

- Managing the Internal Audit Activity;
- Nature of Work;
- Engagement Planning;
- Performing the Engagement;
- Communicating Results;
- Monitoring Progress; and
- Communicating the Acceptance of Risks.

## 2. Self-Assessment Process

2.1 As previously agreed with Members of the Audit Committee, a self-assessment was undertaken in February 2024 to assess the level of compliance with the PSIAS and to identify further work required to comply with the Standards.

2.2 A self-assessment was undertaken by the Chief Internal Auditor with input, challenge and support from the Group Auditors.

2.3 This report summarises the results of the self-assessment, specifically detailing the areas of non and partial compliance and identifies the next steps in achieving compliance (where appropriate).

2.4 We have not reported the areas of full compliance.

## 3. Self-Assessment Results

3.1 The checklist for assessing conformance with the PSIAS identifies 344 standards in the form of questions against which an assessment as to the level of compliance is made.

3.2 The following table summarises the results of the self-assessment:

| Summary of Responses: | Count: |
|---|---|
| Compliant | 308 |
| Partial Compliance | 13 |
| Not Compliant | 1 |
| Not Applicable | 22 |
| **Total** | **344** |

3.3 The following sections detail the areas of non and partial compliance and identify the next steps in achieving compliance (where appropriate).

3.4 For the purposes of the standard, the Chief Audit Executive (CAE) is the Chief Internal Auditor, and the Board is the Audit Committee.

## 4. Area of Non-Compliance

### Fraud Risk Assessment

4.1 It is a requirement of the Standards that the Internal Audit activity evaluates the potential for fraud and also how the organisation itself manages fraud risk.

| |
|---|
| **Response:**<br><br>We are not aware of a fraud risk assessment being conducted and we have not yet evaluated the organisations controls to manage this risk. Plans are in place to complete a fraud risk assessment as part of the 2024/25 Internal Audit Plan and we will undertake further work to evaluate how the organisation itself manages fraud risk. |

## 5. Areas of Partial Compliance

### Board Oversight

5.1 The Standards require the Board to approves the internal audit budget and resource plan.

| |
|---|
| **Response:**<br><br>In common with most other local authorities, the number of audit plan days is approved by the Audit Committee, but not the financial budget. Approval of the budget is not specifically performed by the Board, as this is considered to be a management activity, however, in agreeing the audit plan and the associated number of days, the Board is able to satisfy itself as to the level of audit coverage. |

5.2 There is a requirement for feedback to be sought from the chair of the audit committee for the CAE's performance appraisal.

| |
|---|
| **Response:**<br><br>The Audit Committee terms of reference includes a requirement to undertake a review of the effectiveness of Internal Audit, which would identify any feedback about the Chief Internal Auditors performance. Any concerns by the Chair of the Audit Committee should be raised with the Section 151 Officer. However, there is no formal process to pick up |

feedback from the Audit Committee Chair within the Chief Internal Auditor's Performance & Development discussions, this is common with other local authorities.

**External Assessment**

5.3 There were eight areas of partial compliance which relate to the arrangements and reporting of the results of an independent External Assessment, we have marked these as being partially compliance for full transparency, but they could be considered not yet required. These areas of partial compliance include the need to:

- ensure an external assessment been carried out, or is planned to be carried out, at least once every five years;
- discuss the proposed form of the external assessment and the qualifications and independence of the assessor or assessment team with the board;
- agree the scope of the external assessment with an appropriate sponsor, such as the chair of the audit committee, the Chief Finance Officer or the Chief Executive;
- ensure the assessor or assessment team demonstrate its competence in both areas of professional practice of internal auditing and the external assessment process;
- ensure the CAE has used his or her professional judgement to decide whether the assessor or assessment team demonstrates sufficient competence to carry out the external assessment;
- manage any real or potential conflicts of interest of the assessor or assessment team;
- report the results of the activity to senior management and the board.

**Response:**

There is no evidence of an external assessment being undertaken in the past five years. Plans are in place to undertake an external assessment once the service is transferred to Orbis IA (a service which has already been confirmed as being fully conforming with the Standards), the results of which will be reported to the Audit Committee and the areas with Appendix A will then be addressed.

**Other sources of assurance**

5.4 The standards require the internal audit plan to take into account the organisation's assurance framework, and to ensure the audit planning approach identifies and relies on other sources of assurance. Further the Chief Audit Executive is required to carry out an assurance mapping exercise as part of identifying and determining the approach to using other sources of assurance.

**Response:**

Identification and assessment of other sources of assurance is picked up through liaison with key stakeholders and built into our audit planning process. It is however recognised that this is an area for improvement and further work will be carried out to evaluate the extent to which Internal Audit can rely on the assurance of other providers in planning its activity.

## 6. Next Steps

6.1 As part of the transition to Orbis, work will continue to develop and improve the Hastings Borough Council Internal Audit service with a view to bringing it fully in line with professional standards. It is anticipated that much of this will be achieved by applying existing Orbis IA principles and working practices to the service, given these are already confirmed to be in full conformance. Further updates will be reported to the Audit Committee as part of future Internal Audit progress reports.

Mark Winton
Chief Internal Auditor
February 2024

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# Agenda Item 7

| | |
|---|---|
| **Report To:** | **Audit Committee** |
| **Date of Meeting:** | **7 March 2024** |
| **Report Title:** | **Treasury Management Strategy and Capital Strategy 2024/25** |
| **Report By:** | **Kit Wheeler** |
| | **Chief Finance Officer** |
| **Key Decision:** | **Yes** |
| **Classification:** | **Open** |

## Purpose of Report

To consider the draft Treasury Management Strategy, Annual Investment Strategy, Minimum Revenue Provision (MRP) Policy and Capital Strategy and make recommendations to full Council as appropriate.

This is to ensure that there is an effective framework for the management of the Council's investments, cash flows and borrowing activities prior to the start of the new financial year.

The Council is expected to have £64.9 million of external debt (as at 31 March 2024), and there is no planned increase in the level of debt for 2024/25.

## Recommendations

**Audit Committee recommends to Cabinet and full Council that:**

**A. The Council approve the Treasury Management Strategy, Minimum Revenue Provision (MRP) Policy, Annual investment Strategy.**

**B. Note the draft Capital Strategy.**

**C. The strategies listed are updated as necessary during 2024/25 in the light of changing and emerging risks and the Council's evolving future expenditure plans.**

## Reasons for Recommendations

1. The Council seeks to minimise the costs of borrowing and maximise investment income whilst ensuring the security of its investments.

2. The 2024/25 Budget included significant reductions in the Capital Programme to help the Council address its financial deficit including agreeing to asset sales, with the primary focus being on financial stability and addressing the housing crisis.

3. The CIPFA Treasury Management Code of Practice, previously adopted by the Council, takes account of the more commercialised approach being adopted by councils and the enhanced levels of transparency required. The Code has represented best practice and helps ensure compliance with statutory requirements.

4. The Council can diversify its investments and must carefully consider the level of risk against reward. Investments can help to close the gap in the budget in the years ahead and thus help to preserve services, assist in the regeneration of the town, provide additional housing, and enhance the long-term sustainability of the town. However, over reliance on such income streams would involve taking unnecessary risks with the future of the Council and its ability to deliver statutory services.

## Introduction

5. The Council is required to operate a balanced budget, which broadly means that cash raised will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

6. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing needs of the Council, essentially the longer-term cash flow planning to ensure the Council can meet its capital spending operations. This management of longer-term cash may involve arranging long or short-term loans, or using longer term cash flow surpluses, and on occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

7. The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity and the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget.  Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will result in a loss to the General Fund balances.

8. Treasury management in this context is defined by CIPFA as:

   ***"The management of the organisation's borrowing, 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 optimum performance consistent with those risks"***

9. This report and subsequent strategy has been delayed, owing to the substantial changes to the Capital programme as a result of the decision around the sale of Cornwallis site on 29 January at Cabinet. This has such a material impact on the Councils financial position and therefore the Treasury Management Strategy that it needed to be completed after that decision had been agreed.

## Revisions to the Prudential Code and Treasury Management Code

10. CIPFA published the revised Codes on 20th December 2021 and has stated that revisions need to be included in the reporting framework from the 2023/24 financial year and has been applying these changes throughout 2023/24 financial year as reported to Audit Committee on a Quarterly basis through the regular reporting cycle.

11. The Treasury Management Strategy details the requirements of the code.

## Borrowing / Borrowing Levels

## Investment guidance

12. The Treasury Management Code requires all investments and investment income to be attributed to one of the following three purposes: -

    **Treasury management**
    Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

    **Service delivery**
    Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose".

    **Commercial return**
    Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to an authority's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

## The Primary Requirements of the Code

13. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

14. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

15. Receipt by the full Council of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Capital Strategy, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.

16. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

17. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Council the delegated body is the Audit Committee.

18. Publication of the Strategies on the Council's website.

## Reporting Arrangements

19. The reporting arrangements proposed, in accordance with the requirements of the Code, are summarised below:-

| **Area of Responsibility** | **Council/ Committee/ Officer** | **Frequency** |
|---|---|---|
| Treasury Management Strategy / Annual Investment Strategy / MRP policy/ Capital Strategy (in future years) | Cabinet and Council | Annually before the start of the year |
| Treasury Management Strategy / Annual Investment Strategy / Capital Strategy/MRP policy – Mid Year report | Cabinet and Council | Mid-year |
| Treasury Management Strategy/Capital Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times | Cabinet and Council | As required |
| Annual Treasury Outturn Report | Cabinet and Council | Annually by 30 September after the end of the year |
| Treasury Management Practices | S151 Officer | Reviewed as required (minimum - annually) |

| | | |
|---|---|---|
| Scrutiny of Treasury Management Strategy | Audit Committee | Annually before the start of the year |
| Scrutiny of treasury management performance and strategy | Audit Committee | Quarterly Monitoring reports, Mid-Year report, |

20. The CIPFA Code of Practice on Treasury Management (2021) was adopted by this Council in February 2022. The main clauses adopted are included in Appendix 8.

21. The Audit Committee is required to consider the Prudential Indicators as part of the Treasury Management Strategy and make recommendations to Cabinet and full Council; these are identified in the report and Appendix 4 of the Treasury Management Strategy.

## Capital Strategy

The Capital strategy is currently in draft form and requires further discussion. It will be revised after the Asset Management Plan is completed.

22. In the light of the increasing commercialisation within local government in particular, in December 2017, CIPFA issued revised Prudential and Treasury Management Codes. The codes require all local authorities to produce detailed Capital Strategies.

23. The Capital Strategy is intended to give a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services along with an overview of how associated risk is managed and the implications for future financial sustainability.

24. The development of such a strategy allows flexibility to engage with full council to ensure that the overall strategy, governance procedures and risk appetite are fully understood by all elected members.

25. The Capital Strategy should be tailored to the authority's individual circumstances but should include capital expenditure, investments and liabilities and treasury management. The Capital Strategy should include sufficient detail to allow all members to understand how stewardship, value for money, prudence, sustainability, and affordability will be secured and to meet legislative requirements on reporting.

26. The Capital strategy being a high-level document that summarises in appropriate detail the requirements for specific investment appraisals. As a minimum such requirements being:

- The capital schemes that are proposed and their objectives
- The legal power to undertake a particular scheme
- The key aspects of the financial appraisal, including any significant risks that have been identified
- Qualitative criteria that have underpinned the recommendation for a scheme to proceed e.g. links to Corporate plan, economic growth, job retention, etc.
- Likely source of funding
- Long term implications

- Risks and affordability

27. In assessing new income generating proposals the Council does already consider the above list of issues as part of the due diligence checklist and decisions are fully documented.

28. This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset.

29. The Capital Strategy looks to cover a much longer planning period than the existing capital programme. The future expenditure plans continue to evolve. The capital strategy and all the prudential indicators and controls are attached for the known schemes. Borrowing limits will need to be determined by full Council based on affordability and risk in due course.

30. Given the timing of the Cornwallis decision and its impact on the Capital Programme as well as the upcoming new Asset Strategy Plan the Capital Strategy will be updated in the new financial to take account of any changes and recommendations that come out as part of that strategy to ensure there is a clear link between all strategies for the Council.

## Risk Management

31. The Investment strategy prioritises security of investments over return. Where investments are made, they are limited in size and duration. External treasury advisers are used to advise the Council and have been used to train members. The Council has introduced further checks on credit worthiness of counterparties over the years as and when these have been further developed by its advisers.

32. Whilst there is no absolute security for investments made, the Council has limited its investments to the higher rated institutions, in order to mitigate the risk as far as practical and looks to reduce the risk by spreading its investment portfolio. The Council has adopted the CIPFA Code of Practice.

33. The CIPFA Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

34. The training needs of treasury management officers will also be reviewed in the light of the Code’s requirements and experience of new staff.

35. The additional risks that the Council has taken on with commercial property, housing and energy investments needs to be considered in the context of the totality of risk that the Council faces e.g. unexpected expenditure demands, robustness of income streams, loans and guarantees to other parties, economic downturns, pandemics etc. Where there is more risk and volatility in income streams, the Council will need to ensure that it maintains sufficient reserves to ensure the Council’s ability to deliver

key services is not jeopardised.

36. The Council spreads its risk on investments by limiting the amount of monies with any one institution or group and limiting the timeframe of the exposure. In determining the level of the investment and period the Council considers formal credit ratings (Fitch) along with its own advisers (Link Group) ratings advice.

37. The security of the principal sum remains of paramount importance to the Council and it has a good history of protecting this investment income to date.

## Economic/Financial Implications

**38.** The Council generally has investments in the year of between £15 million and £35 million at any one time and is estimated to have longer term borrowings of £64.9m by the end of March 2024 (if no further external borrowing is undertaken). Management of its investments, borrowing and cash flow remains crucial to the proper and effective management of the Council. The Strategies and Policies detailed in the report directly influence the Council's Medium Term Financial Strategy and the annual budget.

### Organisational Consequences

39. The Cabinet is responsible for the development and review of the Treasury Management Strategy, Minimum Revenue Provision (MRP) Policy, Investment Strategy and the future Capital Strategy. The Audit Committee is responsible for scrutinising these strategies, policies and performance throughout the year. Full Council, as the budget setting body, remains responsible for the approval of the Treasury Management Strategy, MRP Policy, and Investment Strategy and for the Capital Strategy.

40. Monitoring reports will be produced and will be presented to Cabinet and the Audit Committee. A mid-year report is presented to full Council on any concerns arising since approving the initial strategies and policies. Only full Council will be able to amend the Treasury Management Strategy, MRP Policy, Investment Strategy or Capital Strategy. The Chief Finance Officer will determine the Treasury Management Practices and associated schedules.

41. There are responsibilities placed on the Council and the Chief Finance officer from the 2021 Codes of Practice which relate to governance arrangements, ensuring robustness of business cases, and risk management.

42. The risk management requirements relate to asset related properties which the Council has borrowed to finance, and assessments of overall risk.

43. There are specific requirements to maintain schedules of counterparties and of any guarantees that the Council may give or have given in the past in order to fully assess the potential risks that the Council may be exposed to when making investment decisions.

### Timetable of Next Steps

Please include a list of key actions and the scheduled dates for these:

| Action | Key milestone | Due date (provisional) | Responsible |
|---|---|---|---|
| Arrange Training for new and existing members / officers | For Mid-Year Review and prior to setting strategies for the forthcoming year Report | July 2024<br><br>&<br><br>January 2025 | Chief Finance Officer |

**Wards Affected**

None

**Policy Implications**

| | |
|---|---|
| Equalities and Community Cohesiveness | No |
| Crime and Fear of Crime (Section 17) | No |
| Risk Management | Yes |
| Environmental Issues & Climate Change | No |
| Economic/Financial Implications | Yes |
| Human Rights Act | No |
| Organisational Consequences | Yes |
| Local People's Views | No |
| Anti-Poverty | No |
| Legal | No |

**Additional Information**

Documents Attached:

(i)Treasury Management Strategy (including Investment Strategy)

Includes the following Appendices:-

1. MRP Introduction and Policy Statement
2. Interest Rate Forecasts
3. Economic Review
4. Prudential and Treasury Indicators
5. Specified and non-Specified Investments
6. Approved Countries for Investments
7. Treasury Management Policy Statement
8. Purpose and Requirements of the Code
9. Treasury Management Scheme of Delegation
10. The Treasury Management Role of the Section 151 Officer

(ii) Draft Capital Strategy

(iii) Glossary of Terms

Other Supporting Documents:-

CIPFA - Treasury Management Code of Practice (2021)
CIPFA - The Prudential Code (2021)
Budget Report - Cabinet 12 February 2024

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# Treasury Management Strategy Statement 2024/25

## Minimum Revenue Provision Policy Statement and Annual Investment Strategy

**Introduction**

1. The Local Government Act 2003 (the Act) and supporting regulations require the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent, and sustainable.
2. The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy; this sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments. There is also the requirement to produce a Capital Strategy – also for determination by full Council.
3. The Treasury Management strategy covers two main areas:

   (i) Capital issues:
   - the capital plans (in summarised form) and the prudential indicators,
   - the Minimum Revenue Provision (MRP) policy.

   (ii) Treasury management issues:
   - the current treasury position,
   - treasury indicators which limit the treasury risk and activities of the Council,
   - prospects for interest rates,
   - the borrowing strategy,
   - policy on borrowing in advance of need,
   - debt rescheduling,
   - the investment strategy,
   - creditworthiness policy, and
   - policy on use of external service providers.
4. These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, DLUHC MRP Guidance, the CIPFA Treasury Management Code and DLUHC Investment Guidance.
5. It should be noted that DLUHC is proposing to tighten up regulations around local authorities financing capital expenditure on investments in commercial projects for yield and has already closed access to all PWLB borrowing if such schemes are included in an authority's capital programme. The CIPFA codes have adopted a similar outlook to discourage further capital expenditure on commercial investments for yield.
6. DLUHC is also finalising a consultation on amending MRP regulations/guidance for England, it is likely that any changes will take effect from 2024/25 at the earliest.
7. The strategy for 2024/25 in respect of the following aspects of the treasury management function is based upon the Council officers' views on interest rates, supplemented with leading market forecasts provided by the Council's treasury advisor, Link Group.

**Revisions to the Prudential Code and Treasury Management Code**

8. CIPFA published the revised Codes on 20th December 2021 and has stated that revisions

need to be included in the reporting framework from the 2023/24 financial year. The Council, therefore, has to have regard to these Codes of Practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to full Council for approval.

9. The revised Treasury Management Code requires all investments and investment income to be attributed to one of the following three purposes:

**Treasury Management**

Arising from the organisation's cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

**Service Delivery**

Investments held primarily and directly for the delivery of public services including housing, regeneration, and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in cases where the income is "either related to the financial viability of the project in question or otherwise incidental to the primary purpose."

**Commercial Return**

Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to an authority's financial capacity – i.e., that 'plausible losses' could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

10. The revised Treasury Management Code requires an authority to implement the following:

1. **Adopt a new liability benchmark treasury indicator** to support the financing risk management of the capital financing requirement; this is to be shown in chart form for a minimum of ten years, with material differences between the liability benchmark and actual loans to be explained.
2. **Long-term treasury investments**, (including pooled funds), are to be classed as commercial investments unless justified by a cash flow business case.
3. **Pooled funds** are to be included in the indicator for principal sums maturing in years beyond the initial budget year.
4. Amendment to the **knowledge and skills register** for officers and members involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each authority.
5. **Reporting to members is to be done quarterly.** Specifically, the Chief Finance Officer (CFO) is required to establish procedures to monitor and report performance against all forward-looking prudential indicators at least quarterly. The CFO is expected to establish a measurement and reporting process that highlights significant actual or forecast deviations from the approved indicators. However, monitoring of prudential indicators, including forecast debt and investments, is not required to be taken to full Council and should be reported as part of the authority's integrated revenue, capital, and balance sheet monitoring.
6. **Environmental, social and governance (ESG)** issues to be addressed within an authority's treasury management policies and practices (TMP1).

11. The main requirements of the Prudential Code relating to service and commercial investments are:

1. The risks associated with service and commercial investments should be proportionate to their financial capacity, i.e., that plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services.

2. An authority must not borrow to invest for the primary purpose of commercial return.
3. It is not prudent for local authorities to make any investment or spending decision that will increase the CFR, and so may lead to new borrowing, unless directly and primarily related to the functions of the authority, and where any commercial returns are either related to the financial viability of the project in question or otherwise incidental to the primary purpose.
4. An annual review should be conducted to evaluate whether commercial investments should be sold to release funds to finance new capital expenditure or refinance maturing debt.
5. A prudential indicator is required for the net income from commercial and service investments as a proportion of the net revenue stream.
6. Create new Investment Management Practices to manage risks associated with non-treasury investments, (similar to the current Treasury Management Practices).

12. The authority's Capital Strategy or Annual Investment Strategy should include:

1. The authority's approach to investments for service or commercial purposes (together referred to as non-treasury investments), including defining the authority's objectives, risk appetite and risk management in respect of these investments, and processes ensuring effective due diligence.
2. An assessment of affordability, prudence, and proportionality in respect of the authority's overall financial capacity (i.e., whether plausible losses could be absorbed in budgets or reserves without unmanageable detriment to local services).
3. Details of financial and other risks of undertaking investments for service or commercial purposes and how these are managed.
4. Limits on total investments for service purposes and for commercial purposes respectively (consistent with any limits required by other statutory guidance on investments).
5. Requirements for independent and expert advice and scrutiny arrangements (while business cases may provide some of this material, the information contained in them will need to be periodically re-evaluated to inform the authority's overall strategy).
6. State compliance with paragraph 51 of the Prudential Code in relation to investments for commercial purposes, in particular the requirement that an authority must not borrow to invest primarily for financial return.

13. This Treasury Management Strategy Statement and Annual Investment Strategy deals solely with treasury management investments, the categories of service delivery and commercial investments are addressed as part of the Capital Strategy.

14. However, as investments in commercial property have implications for cash balances managed by the treasury team, a high-level summary of the impact that commercial investments have, or may have, if it is planned to liquidate such investments within the three-year time horizon of this report.

**Background**

15. The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

16. The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, essentially the longer-term cash flow planning, to ensure that it can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using longer-term cash flow surpluses. On occasion, when it is prudent and

economic, any debt previously drawn may be restructured to meet risk or cost objectives.

17. The contribution the treasury management function makes to the Council is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

18. CIPFA defines treasury management as:

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

19. Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day-to-day treasury management activities.

**Reporting Requirements**

**Capital Strategy**

20. The CIPFA 2021 Prudential and Treasury Management Codes require all local authorities to prepare a Capital Strategy report which will provide the following:

- a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services,
- an overview of how the associated risk is managed,
- The implications for future financial sustainability.

21. The aim of the strategy is to ensure that all the Councils' elected members fully understand the overall long-term policy objectives and resulting Capital Strategy requirements, governance procedures and risk appetite.

**Treasury Management Reporting**

22. The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

a. **Prudential and treasury indicators and treasury strategy** (this report) - The first, and most important report is forward looking and covers:

- the capital plans, (including prudential indicators),
- a minimum revenue provision (MRP) policy, (how residual capital expenditure is charged to revenue over time),
- the Treasury Management Strategy, (how the investments and borrowings are to be organised), including treasury indicators, and
- an Annual Investment Strategy, (the parameters on how investments are to be managed).

b. **A mid-year treasury management report** – This is primarily a progress report and will update members **on** the capital position, amending prudential indicators as necessary, and **whether** any policies require revision. In addition, the Council will report performance against all forward-looking prudential indicators quarterly as part of the quarterly budget monitoring process.

c. **An annual treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

**Scrutiny**

23. The above reports are required to be adequately scrutinised before being recommended to the full Council. This role is undertaken by the Audit Committee.

**Quarterly reports**

24. In addition to the three major reports detailed above, from 2024/25 quarterly reporting (end of June/end of December) is also required. However, these additional reports do not have to be reported to full Council but do require to be adequately scrutinised. The Overview & Scrutiny Committee undertake this role.

**Treasury Management Strategy for 2024/25**

25. The strategy for 2024/25 covers two main areas:

**Capital issues:**

- the capital expenditure plans and the associated prudential indicators.
- the minimum revenue provision (MRP) policy.

**Treasury management issues**

- the current treasury position.
- treasury indicators which limit the treasury risk and activities of the Authority.
- prospects for interest rates.
- the borrowing strategy.
- policy on borrowing in advance of need.
- debt rescheduling.
- the investment strategy.
- creditworthiness policy; and
- the policy on use of external service providers.

26. These elements cover the requirements of the Local Government Act 2003, DLUHC Investment Guidance, DLUHC MRP Guidance, the CIPFA Prudential Code and the CIPFA Treasury Management Code.

**Training**

27. The CIPFA Treasury Management Code requires the responsible officer to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny.

28. Furthermore, pages 47 and 48 of the Code state that they expect "all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance, and decision making.

29. As a minimum, authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and board/council members.
- Require treasury management officers and board/council members to undertake self-assessment against the required competencies (as set out in the schedule that may be adopted by the organisation).
- Have regular communication with officers and board/council members, encouraging them to highlight training needs on an ongoing basis."

30. The training needs of treasury management officers are periodically reviewed.

31. A formal record of the training received by officers central to the Treasury function will be maintained by People and Places. Similarly, a formal record of the treasury

management/capital finance training received by members will also be maintained by the Chief Finance Officer.

32. Treasury Management Training was offered to all members on 11th January 2023 with further training arranged, as required.

**Treasury Management Consultants**

33. The Authority uses Link Group, Link Treasury Services Limited as its external treasury management advisors.

34. The Authority recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon the services of our external service providers. All decisions will be undertaken with regards to all available information, including, but not solely, our treasury advisers.

35. It also recognises that there is value in employing external providers of treasury management services to acquire access to specialist skills and resources. The Authority will 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.

**PRUDENTIAL INDICATORS AND TREASURY LIMITS FOR 2023/24 TO 2025/26**

36. The Council's capital expenditure plans are the key driver of treasury management activity. The output of the capital expenditure plans is reflected in the prudential indicators, which are designed to assist members' overview and confirm capital expenditure plans.

**The Council's Capital Position (Prudential Indicators)**

37. The prudential code requires the local authority to identify prudential indicators that enable members, officers, and the public to make a meaningful judgement on the Council's total exposure from borrowing and investment decisions. The indicators are required to cover both the Council's current position and the expected position assuming all planned investments in the forthcoming years are completed.

**Capital Expenditure and Financing**

38. This prudential indicator is a summary of the Council's capital expenditure plans, both those agreed previously, and those forming part of this budget cycle. The table below summarises how the capital expenditure plans and how these are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

| | Actual 2022/23 £'000s | Budget 2023/24 £'000s | Forecast 2023/24 £'000s | Budget 2024/25 £'000s | Budget 2025/26 £'000s | Budget 2026/27 £'000s |
|---|---|---|---|---|---|---|
| **Capital Expenditure** | **9,661** | **22,194** | **17,144** | **12,652** | **6,090** | **3,799** |
| ***Financed by:*** | | | | | | |
| Capital receipts | 3,778 | 952 | 2,579 | 5,130 | 300 | 50 |
| Capital grants | 5,883 | 3,533 | 8,907 | 4,861 | 2,433 | 2,064 |
| Reserves | 0 | 0 | 271 | 0 | 0 | 0 |
| Revenue | 0 | 0 | 0 | 0 | 0 | 0 |
| **Net financing need for the year** | **0** | **17,709** | **5,387** | **2,661** | **3,357** | **1,685** |

39. Other long-term liabilities - the above financing need excludes other long-term liabilities, such as PFI and leasing arrangements that already include borrowing instruments.

40. The schemes in the capital programme which may require additional financing (at least in part) in 2024/25 are:

- Housing Acquisition Programme 50 units of Temporary Accommodation (£4.7m)

- Energy generation - Unallocated (£1m)
- Roof Refurbishment programme (£700k)
- Energy – Solar Panels (£500k)
- Priory Meadow Contribution to Capital Works (£250k)
- Restoration of Pelham Crescent / Pelham Arcade (£340k)
- Groyne Refurbishment (£35k)

**Borrowing Needs (the Capital Financing Requirement)**

41. The second prudential indicator is the Council's Capital Financing Requirement (CFR). The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's indebtedness and so its underlying borrowing need. Any capital expenditure above, which has not immediately been paid for through a revenue or capital resource, will increase the CFR.

42. The CFR does not increase indefinitely, as the minimum revenue provision (MRP) is a statutory annual revenue charge which broadly reduces the indebtedness in line with each asset's life, and so charges the economic consumption of capital assets as they are used.

43. The CFR includes any other long-term liabilities (e.g., PFI schemes, finance leases). Whilst these increase the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility by the PFI, PPP lease provider and so the Council is not required to separately borrow for these schemes. The Authority currently has no such schemes within the CFR.

44. The Council is asked to approve the CFR projections below, the table provides an estimate of the Council's Capital Financing Requirement (CFR) for the current and next 3 years.

**Table 1 - Capital Financing Requirement (CFR)**

| CFR | 2022/23 (Unaudited) £'000s | 2023/24 (Estimate) £'000s | 2024/25 (Estimate) £'000s | 2025/26 (Estimate) £'000s | 2026/27 (Estimate) £'000s |
|---|---|---|---|---|---|
| CFR-Opening | 71,970 | 71,099 | 70,195 | 69,229 | 68,208 |
| Less MRP | (870) | (904) | (966) | (1,021) | (1,125) |
| Plus, New Borrowing | - | - | - | - | - |
| **CFR Closing** | 71,099 | 70,195 | 69,229 | 68,208 | 67,083 |

45. The Council has at the time of writing, c£64.9m of PWLB debt. To borrow for the remainder of the 2023/24 capital programme i.e., up to the projected level of the CFR (£70.1m) it would need to fund a further £5.3m by the end of March 2024. The Capital Financing Requirement will gradually decrease over the next few years. It is expected to reach £68.7m by 2026/27 (based on the capital programme).

46. As a key indicator the Council needs to ensure that its gross debt does not, except in the short term, exceed the total of the Capital Financing Requirement (CFR) in the preceding year plus the estimates of any additional CFR for 2024/25 and the following two financial years. This allows some flexibility for limited early borrowing for future years but ensures that borrowing is not undertaken for revenue or speculative purposes.

47. The total CFR can also be reduced by:

    (i) the application of additional capital financing resources (such as unapplied capital receipts), or

    (ii) charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

48. The Council had achieved a near fully funded position at the start of 2022/23. This means that the capital borrowing need (the Capital Financing Requirement), has been fully funded

with loan debt. This strategy had been considered prudent as borrowing costs had been increasing. However, there is a cost of doing this as investment returns albeit currently higher than in previous years are unlikely to remain at current levels.

49. During 2021/22 and much of 2022/23, interest rates on were on the rise, thus there was a strong case to not borrow externally. until we really had to, i.e., temporarily. This was the strategy that was proposed for 2023/24 (as far as practical) and has saved on borrowing costs and assisted the Council's revenue account. There is however only a limited ability to do this given the depletion of Council reserves, and funds already invested for longer periods.

50. For 2023/24 the Council started the year with internal borrowing of £5.4m - cash supporting the Council's reserves balances and cash flow has been used as a temporary measure to fund Capital expenditure. With recent interest rate increases, and forecast that they will remain static, or fall slightly in the short to medium term, the Council will need to continue to minimise external borrowing.

51. To finance the future Capital program, it is envisaged that no new long-term external borrowing will be required by the Council. The key consideration is the level of internal borrowing. The Chief Finance Officer will make these decisions in conjunction with advice and guidance from our treasury advisors. Current guidance suggest that interest rates have peaked, and will remain at current levels, the short, so the strategy will be to utilise internal borrowing as much as possible to see us through until an expected lower rate environment. Where borrowing is required the option of borrowing short-term will be considered rather than locking into to higher rates for a prolonged period. Some longer-term borrowing might be required and will be advantageous where affordable as it reduces the risk of future adverse movements in interest rates.

52. The table below highlights the Council's projected gross borrowing position against the CFR (showing the level that is financed from internal borrowing).

**Table 2 - Council's Projected Gross Borrowing Position Against the CFR**

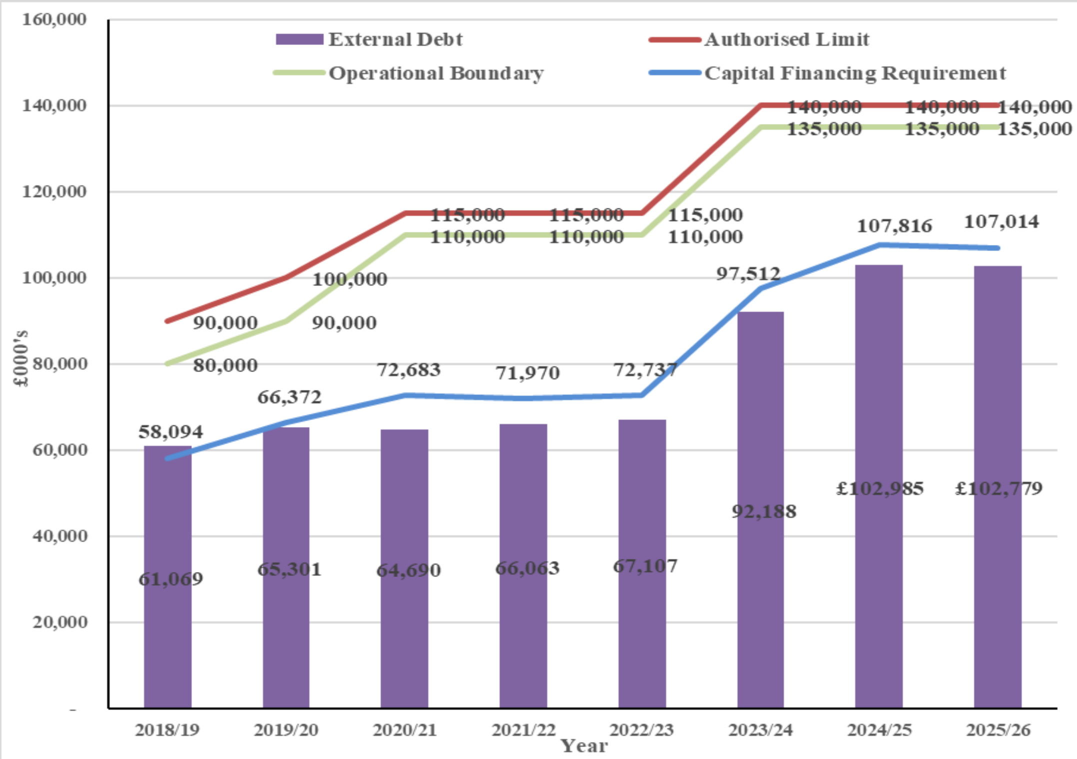
| Internal Borrowing | 2023/24 Forecast £000's | 2023/24 Estimate £000's | 2024/25 Estimate £000's | 2025/26 Estimate £000's |
|---|---|---|---|---|
| Capital Financing Requirement (CFR) | 71,099 | 70,195 | 69,229 | 68,208 |
| External Funding | 65,712 | 67,534 | 65,872 | 66,523 |
| **Net Internal Funding** | **5,387** | **2,661** | **3,357** | **1,685** |

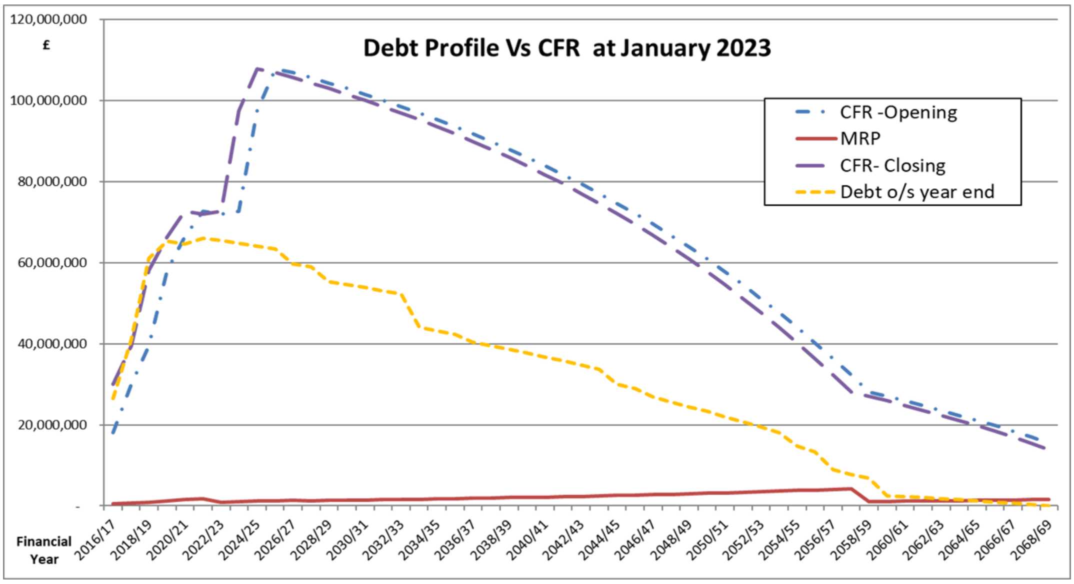
53. The Council is now (20 January 2024) maintaining an under-borrowed position. Borrowing activity is constrained by prudential indicators particularly the CFR, and by the authorised limit. The Council's long-term borrowing must only be for a capital purpose. This essentially means that the Council cannot borrow to support revenue expenditure.

### Debt Profile and CFR

54. The graph below shows how the CFR (blue and purple lines) reduce over time as MRP payments are made. The yellow line shows the level of external debts reducing as principal repayments are made (see debt maturity graph below).

**Table 3 - External Debt, Authorised Limits and CFR Projections**




55. The graph above is based on the current known capital programme up to 2026/27. If further capital expenditure is finance by borrowing, which is highly likely, then this will push the trajectory of the graph out into further years and increase future MRP payment.

### Liability Benchmark

56. The Authority is required to estimate and measure the Liability Benchmark (LB) for the forthcoming financial year and the following two financial years, as a minimum.

57. There are four components to the LB:

- **Existing loan debt outstanding**: the Authority's existing loans that are still outstanding in future years.
- **Loans CFR**: this is calculated in accordance with the loans CFR definition in the Prudential Code and projected into the future based on approved prudential borrowing and planned MRP.
- **Net loans requirement**: this will show the Authority's gross loan debt less treasury management investments at the last financial year-end, projected into the future and based on its **approved** prudential borrowing, planned MRP and any other major cash flows forecast.
- **Liability benchmark** (or gross loans requirement): this equals net loans requirement plus short-term liquidity allowance.

**Core Funds and Expected Investment Balances**

58. The application of resources (capital receipts, reserves etc.) to either finance capital expenditure or other budget decisions to support the revenue budget will have an ongoing impact on investments unless resources are supplemented each year from new sources (asset sales etc.). Detailed below are estimates of the year-end balances for each resource and anticipated day-to-day cash flow balances.

59. The treasury indicators for borrowing activity are the **Authorised Limit** and the **Operational Boundary** for external debt.

60. The **Authorised Limit**, which is a limit beyond which external debt is prohibited, needs to be set or revised by the full Council; it is a statutory duty under Section 3 (1) of the Local Government Act 2003 and supporting regulations. It reflects the level of borrowing which, while not desired, could be afforded in the short term. It is the expected maximum borrowing need with some headroom for unexpected movements.

| **Authorised Limit** | **2022/23** | **2023/24** | **2024/25** | **2025/26** | **2026/27** |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| Debt | 110,000 | 135,000 | 135,000 | 135,000 | 135,000 |
| Other long-term liabilities | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| **TOTAL** | 115,000 | 115,000 | 140,000 | 140,000 | 140,000 |

61. The **Operational Boundary** is the limit beyond which external debt is not normally expected to exceed.

| **Operational Boundary** | **2022/23** | **2023/24** | **2024/25** | **2025/26** | **2026/27** |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| Debt | 105,000 | 130,000 | 130,000 | 130,000 | 130,000 |
| Other long-term liabilities | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| **TOTAL** | 110,000 | 110,000 | 135,000 | 135,000 | 135,000 |

62. Essentially the Council is required to ensure that total capital investment remains within sustainable limits and, in particular, that the impact upon its future Council Tax levels is 'acceptable.'

63. Whilst termed an "Affordable Borrowing Limit", the capital plans to be considered for inclusion in the Capital programme incorporate financing by both external borrowing as well as other forms of liability e.g., Credit arrangements (such as leases).

64. The Authorised Limit and Operational Boundary are to be set, on a rolling basis, for the forthcoming financial year and two successive financial years by full Council as part of this strategy.

65. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

66. Given the current level of capital expenditure plans for the years ahead it is recommended that the limits are maintained at the existing levels to allow sufficient headroom for our capital aspirations.

**Minimum Revenue Provision (MRP)**

67. Appendix 1 of this report provides the detail on what the MRP is and the basis of the calculation. Basically, authorities are required each year to set aside some of their revenues as provision for debt repayment. Unlike depreciation, which is reversed out of the accounts, this provision has a direct impact on the Council Tax requirement. The provision is in respect of capital expenditure that is financed by borrowing or credit arrangements e.g., leases.

68. The Council is required to make a "Prudent Provision" which basically ensures that revenue monies are set aside to repay the debt over the useful life of the asset acquired i.e., the Minimum Revenue Provision (MRP). This can be achieved by equal annual instalments (current practice) or an annuity method – annual payments gradually increasing over the life of the asset. Where an annuity loan is taken, the Council's policy (Appendix 1) was amended to reflect the matching, as far as possible, of the MRP with the actual principal repaid (within each debt repayment).

69. The MRP for 2024/25 is estimated at £966,000 (the statutory charge to revenue that remains within the accounts).

70. The Government are consulting on amending MRP regulations/guidance for England. One of the revisions likely is to make it clear to all authorities that where loans have been made for capital purposes to other organisations e.g., local authority companies, housing providers, then provision for debt repayments must be made. Hastings BC has always done so and is not caught out by this sensible requirement. The latest information we have is that any changes to the guidance will take effect from 2024/25 at the earliest.

**PROSPECTS FOR INTEREST RATES**

71. The Authority has appointed Link Group as its treasury advisor and part of their service is to assist the Authority to formulate a view on interest rates. Link provided the following forecasts on 08 January 2024. These are forecasts for Bank Rate, average earnings and PWLB certainty rates, gilt yields plus 80 bps.

| Link Group Interest Rate View 08.01.24 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Mar-26 | Jun-26 | Sep-26 | Dec-26 | Mar-27 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| BANK RATE | 5.25 | 5.25 | 4.75 | 4.25 | 3.75 | 3.25 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 3 month ave earnings | 5.30 | 5.30 | 4.80 | 4.30 | 3.80 | 3.30 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 6 month ave earnings | 5.20 | 5.10 | 4.60 | 4.10 | 3.70 | 3.30 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 |
| 12 month ave earnings | 5.00 | 4.90 | 4.40 | 3.90 | 3.60 | 3.20 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.20 | 3.20 |
| 5 yr PWLB | 4.50 | 4.40 | 4.30 | 4.20 | 4.10 | 4.00 | 3.80 | 3.70 | 3.60 | 3.60 | 3.50 | 3.50 | 3.50 |
| 10 yr PWLB | 4.70 | 4.50 | 4.40 | 4.30 | 4.20 | 4.10 | 4.00 | 3.90 | 3.80 | 3.70 | 3.70 | 3.70 | 3.70 |
| 25 yr PWLB | 5.20 | 5.10 | 4.90 | 4.80 | 4.60 | 4.40 | 4.30 | 4.20 | 4.20 | 4.10 | 4.10 | 4.10 | 4.10 |
| 50 yr PWLB | 5.00 | 4.90 | 4.70 | 4.60 | 4.40 | 4.20 | 4.10 | 4.00 | 4.00 | 3.90 | 3.90 | 3.90 | 3.90 |

72. The central forecast for interest rates was previously updated on 7 November and reflected a view that the MPC would be keen to further demonstrate its anti-inflation credentials by keeping Bank Rate at 5.25% until at least H2 2024. We expect rate cuts to start when both the CPI inflation and wage/employment data are supportive of such a move, and when there is a likelihood of the overall economy enduring at least a slowdown or mild recession over the coming months (although most recent GDP releases have surprised with their on-going robustness).

73. Naturally, timing on this matter will remain one of fine judgment: cut too soon, and inflationary pressures may well build up further; cut too late and any downturn or recession may be prolonged.

74. In the upcoming months, our forecasts will be guided not only by economic data releases and clarifications from the MPC over its monetary policies and the Government over its fiscal policies, but also international factors such as policy development in the US and Europe, the

provision of fresh support packages to support the faltering recovery in China as well as the on-going conflict between Russia and Ukraine, and Gaza and Israel.

**Public Works Loan Board (PWLB) Rates**

75. The short and medium part of the gilt curve has rallied since the start of November as markets price in a quicker reduction in Bank Rate through 2024 and 2025 than held sway back then. This reflects market confidence in inflation falling back in a similar manner to that already seen in the US and the Euro-zone. At the time of writing there is c70 basis points difference between the 5- and 50-year parts of the curve.

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

- The overall balance of risks **to** economic growth in the UK is even.

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

- **Labour and supply shortages** prove **more** enduring and disruptive and depress economic activity (accepting that in the near-term this is also an upside risk to inflation and, thus, could keep gilt yields high for longer).
- **The Bank of England** has increased Bank Rate too fast and too far over recent months, and subsequently brings about a deeper and longer UK recession than we currently anticipate.
- **Geopolitical risks,** for example in Ukraine/Russia, the Middle East, China/Taiwan/US, Iran, and North Korea, which could lead to increasing safe-haven flows.

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

- Despite the tightening in Bank Rate to 5.25%, the **Bank of England allows inflationary pressures to remain elevated** for a long period within the UK economy, which then necessitates Bank Rate staying higher for longer than we currently project.
- **The pound weakens** because of a lack of confidence in the UK Government's pre-election fiscal policies, which may prove inflationary, resulting in investors pricing in a risk premium for holding UK sovereign debt.
- Projected **gilt issuance, inclusive of natural maturities and QT,** could be too much for the markets to comfortably digest without higher yields compensating.

**LINK GROUP FORECASTS**

76. We expect the MPC will keep Bank Rate at 5.25% until the second half of 2024, to combat on-going inflationary and wage pressures, even if they have dampened somewhat of late. We do not think that the MPC will increase Bank Rate above 5.25%.

**Gilt yields and PWLB rates**

77. The overall longer-run trend is for gilt yields and PWLB rates to fall back over the timeline of our forecasts, as inflation continues to fall through 2024.

78. Our target borrowing rates are set **two years forward** (as we expect rates to fall back) and the current PWLB (certainty) borrowing rates are set out below:

| PWLB debt | Current borrowing rate as at 08.01.24 p.m. | Target borrowing rate now. (end of Q4 2025) | Target borrowing rate previous. (end of Q3 2025) |
|---|---|---|---|
| 5 years | 4.53% | 3.70% | 3.80% |
| 10 years | 4.67% | 3.90% | 3.80% |
| 25 years | 5.19% | 4.20% | 4.20% |
| 50 years | 4.97% | 4.00% | 4.00% |

79. **Borrowing advice:** Our long-term (beyond 10 years) forecast for Bank Rate remains at 3% and reflects Capital Economics' research that suggests AI and general improvements in productivity will be supportive of a higher neutral interest rate. As all PWLB certainty rates are currently significantly above this level, borrowing strategies will need to be reviewed in that context. Overall, better value can be obtained at the shorter end of the curve and short-dated fixed LA to LA monies should be considered. Temporary borrowing rates will remain elevated for some time to come, but may prove the best option whilst the market continues to factor in Bank Rate reductions for 2024 and later.

80. Our suggested budgeted earnings rates for investments up to about three months' duration in each financial year are set out below.

| Average earnings in each year | Now | Previously |
|---|---|---|
| 2023/24 (residual) | 5.30% | 5.30% |
| 2024/25 | 4.55% | 4.70% |
| 2025/26 | 3.10% | 3.20% |
| 2026/27 | 3.00% | 3.00% |
| 2027/28 | 3.25% | 3.25% |
| 2028/29 | 3.25% | 3.25% |
| Years 6 to 10 | 3.25% | 3.25% |
| Years 10+ | 3.25% | 3.25% |

81. As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

82. Our interest rate forecast for Bank Rate is in steps of 25 bps, whereas PWLB forecasts have been rounded to the nearest 10 bps and are central forecasts within bands of + / - 25 bps. Naturally, we continue to monitor events and will update our forecasts as and when appropriate.

**Borrowing Strategy**

83. The Authority is currently maintaining an under-borrowed position. This means that the capital borrowing need, (the Capital Financing Requirement), has not been fully funded with loan debt as cash supporting the Authority's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as medium and longer dated borrowing rates are expected to fall from their current levels once prevailing inflation concerns are addressed by tighter near-term monetary policy. That is, Bank Rate remains elevated through to the second half of 2024.

84. Against this background and the risks within the economic forecast, caution will be adopted with the 2024/25 treasury operations. The Director of Finance will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances:

- if it was felt that there was a significant risk of a sharp FALL in borrowing rates, then borrowing will be postponed,
- if it was felt that there was a significant risk of a much sharper RISE in borrowing rates than that currently forecast, fixed rate funding will be drawn whilst interest rates are lower than they are projected to be in the next few years.

85. Any decisions will be reported to the appropriate decision-making body at the next available opportunity.

**Current Portfolio Position**

86. The Council's forecast debt position for 31 March 2024, if no further borrowing is taken for the rest of the financial year, as at 15 January 2024, amounted to £65.4m (See Table X below).

**Table 4 - Borrowing**

| Debt | 1 April 2023 Principal | Start Date | Maturity Date | 31 March 2024 Principal | Rate |
|---|---|---|---|---|---|
| PWLB | £7,500,000 | 25/05/2007 | 01/02/2033 | £7,500,000 | 4.80% |
| PWLB | £909,027 | 04/09/2014 | 02/09/2044 | £909,027 | 3.78% |
| PWLB (Optivo) | £1,788,235 | 04/09/2014 | 02/09/2044 | £1,788,235 | 3.78% |
| PWLB (FT)(Annuity) | £95,262 | 21/03/2016 | 20/03/2026 | £79,712 | 1.66% |
| PWLB | £1,000,000 | 11/05/2016 | 11/05/2056 | £1,000,000 | 2.92% |
| PWLB | £1,000,000 | 11/05/2016 | 11/05/2046 | £1,000,000 | 3.08% |
| PWLB | £1,000,000 | 11/05/2016 | 11/05/2036 | £1,000,000 | 3.01% |
| PWLB | £1,000,000 | 11/05/2016 | 11/05/2026 | £1,000,000 | 2.30% |
| PWLB | £2,000,000 | 24/06/2016 | 24/06/2054 | £2,000,000 | 2.80% |
| PWLB | £1,000,000 | 24/06/2016 | 24/06/2028 | £1,000,000 | 2.42% |
| PWLB | £2,000,000 | 21/03/2017 | 21/03/2057 | £2,000,000 | 2.53% |
| PWLB | £2,000,000 | 21/03/2017 | 19/09/2059 | £2,000,000 | 2.50% |
| PWLB | £2,000,000 | 23/03/2017 | 23/03/2060 | £2,000,000 | 2.48% |
| PWLB (Annuity) | £6,652,722 | 01/06/2017 | 01/06/2057 | £6,530,042 | 2.53% |
| PWLB (Annuity) | £7,729,610 | 22/11/2017 | 22/11/2057 | £7,595,155 | 2.72% |
| PWLB | £2,000,000 | 12/12/2018 | 12/06/2028 | £2,000,000 | 1.98% |
| PWLB (Annuity) | £3,756,930 | 13/12/2018 | 13/12/2058 | £3,692,214 | 2.55% |
| PWLB (Annuity) | £2,348,400 | 31/01/2019 | 31/01/2059 | £2,308,028 | 2.56% |
| PWLB (Annuity) | £4,226,034 | 31/01/2019 | 31/01/2069 | £4,177,042 | 2.56% |
| PWLB (Annuity) | £8,827,583 | 20/03/2019 | 20/03/2059 | £8,751,881 | 2.54% |
| PWLB (Annuity) | £4,587,401 | 02/09/2019 | 02/09/2069 | £4,555,098 | 1.83% |
| PWLB | £2,000,000 | 13/01/2022 | 13/01/2062 | £2,000,000 | 1.89% |
| **Total Debt** | **£65,421,204** | | | **£64,887,244** | **2.81%** |

87. The Council has loaned money to four other organisations. Six longer-term loans are outstanding. Namely:

**Table 5 - Loans to Other Organisations**

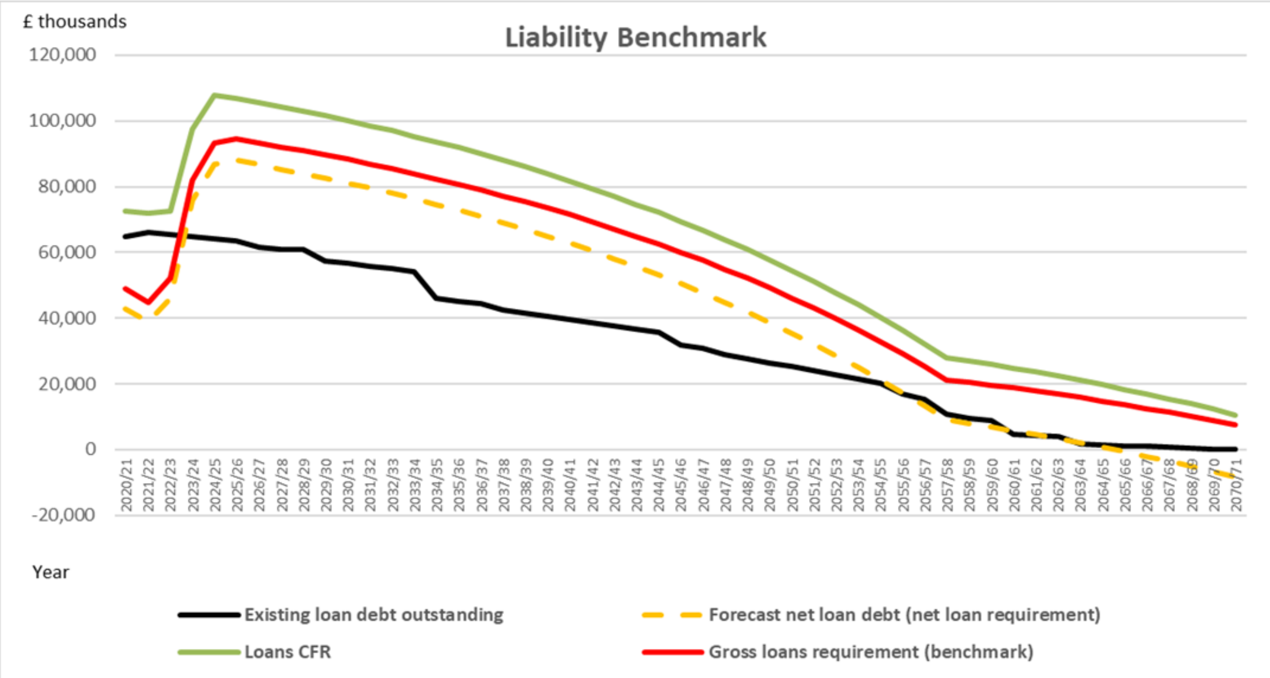
| 3rd Party Organisations | Rate/ Return (%) | Start Date | End Date | Principal Outstanding as at 31/03/2024 £ | Type |
|---|---|---|---|---|---|
| Amicus /Optivo | 3.78% | 04/09/2014 | 02/09/2044 | £1,788,235 | Maturity |
| The Foreshore Trust | 1.66% | 21/03/2016 | 20/03/2026 | £79,712 | Annuity |
| The Source | 2.43% | 17/12/2015 | 17/12/2025 | £8,144 | Annuity |
| | | | **Sub-Total** | **£1,876,091** | |
| **Hastings Housing Company** | | | | | |
| Hastings Housing Company - Loan 1 | 4.48% | 28/02/2018 | 28/02/2058 | £784,676 | Maturity |
| Hastings Housing Company - Loan 2 | 4.84% | 12/02/2019 | 12/02/2059 | £344,810 | Maturity |
| Hastings Housing Company - Loan 3 | 4.84% | 13/06/2019 | 13/06/2059 | £4,359,912 | Maturity |
| | | | **Sub-Total** | **£5,489,398** | |
| | | | **Total** | **£7,365,489** | |

88. Borrowing from the PWLB was taken to fund the Amicus Horizon (now Optivo) loan (£1,788,235 - maturity loan) and the loan to the Foreshore Trust (£300,000 originally

borrowed – annuity loan); these correspond to PWLB loans in Table 1 above. The £25,000 loan to the Source is repayable over a 10-year period and is financed from HBC reserves.

89. Borrowing from the PWLB was taken to fund the loans to Hastings Housing Company Ltd (HHC). The three loans, totalling £5,489,398, are maturity loans and will be due for repayment by HHC at the end of their term.

90. The Liability Benchmark for the Council is shown in the chart below.




91. Some analysis on the lines on the chart above is provided below:

- Existing Loan Debt Outstanding (black line) – The line shows the external loans that the Council has with the PWLB and how the value decreases over time as the principal is repaid.
- Loans CFR (green line) – This line shows the Capital Financing Requirement for the Council. The line decreases as annual MRP payments are made.
- Net Loan Debt (yellow dotted line) – This line shows the Council's debt (CFR) less the value of any external investments it has made i.e., the net debt. You can see that in 2065/66 the line goes below zero and becomes negative. This is because the value of external investments the council is forecasting to be holding is greater that the level of debt that the council has.
- Gross loans requirement (red line) – this line very closely mirrors the Net Loan Debt (yellow dotted) line. It essentially shows the same thing but with an added liquidity allowance – essentially a working balance for the council's treasury activities. This level has been set at £6m to match the councils minimum recommended level of reserves (but in the chart has been inflated by 2% annually so that it maintains its value in real terms).

92. It should be noted that the Liability Benchmark is only a snapshot in time and as capital expenditure plans evolve further borrowing is likely to be incurred which will increase the CFR and push the point at which the lines move towards zero further out into future years.

**Borrowing – Overall Limits**

93. In determining what is a prudent level of borrowing, the Council needs to ensure that it would still be able to provide core services if its investments or income generating initiatives failed

– at least in part. As a guide each £1m of new borrowing, financing an asset with a life of 50 years would currently cost the Council some 5.5% p.a. (based on an annuity loan with a 5% interest rate) i.e., £55,000 p.a.

94. In taking on significant levels of additional debt the Council has to ensure that it can afford to do so. It also needs to ensure that it has an affordable exit strategy in the event that expected returns are not realised. Where property is concerned there is normally an asset to dispose of and such schemes are not therefore at the higher end of the risk spectrum. It is considered that the Council currently has sufficient reserves to ensure that it could dispose of assets in a reasonable period and not be forced into an immediate fire sale. In the event that property values fell by say 20% the Council would not be forced to sell assets providing the rental streams were secure.

**Borrowing – Certainty Rate**

95. The Council again registered for the PWLB certainty rate earlier in the year which has given a 20-basis point reduction in the average rate of borrowing. The Council will look to do so again annually – for as long as it remains available.

**Policy on Borrowing in Advance of Need**

96. The Authority will not borrow more than or in advance of its needs purely in order to profit from the investment of the extra sums borrowed. Any decision to borrow in advance will be within forward approved Capital Financing Requirement estimates and will be considered carefully to ensure that value for money can be demonstrated and that the Authority can ensure the security of such funds.

97. In determining whether borrowing will be undertaken in advance the Council will:

a. ensure that there is a clear link between the capital programme and maturity profile of the existing debt portfolio which supports the need to take funding in advance.

b. ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered.

c. evaluate the economic and market factors that might influence the manner and timing of any decision to borrow.

d. consider the merits and demerits of alternative forms of funding.

e. consider the appropriate funding period.

f. consider the impact of borrowing in advance on temporarily (until required to finance capital expenditure) increasing investment cash balances and the consequent increase in exposure to counterparty risk, and the level of such risks given the controls in place to minimise them.

98. Risks associated with any borrowing in advance activity will be subject to prior appraisal and subsequent reporting through the mid-year or annual reporting mechanism.

**Rescheduling**

99. Rescheduling of current borrowing in our debt portfolio may be considered whilst premature redemption rates remain elevated but only if there is surplus cash available to facilitate any repayment, or rebalancing of the portfolio to provide more certainty is considered appropriate.

100. If rescheduling is to be undertaken, it will be reported to the Cabinet, at the earliest meeting following its action.

**New Financial Institutions as a Source of Borrowing and / or Types of Borrowing**

101. Currently the PWLB Certainty Rate is set at gilts + 80 basis points. However, consideration may still need to be given to sourcing funding from the following sources for the following reasons:

- Local authorities (primarily shorter dated maturities out to 3 years or so – generally still cheaper than the Certainty Rate).

- Financial institutions (primarily insurance companies and pension funds but also some banks, out of forward dates where the objective is to avoid a “cost of carry” or to achieve refinancing certainty over the next few years).
- UK Municipal Bonds Agency and UK Infrastructure Bank

102. Our advisors will keep us informed as to the relative merits of each of these alternative funding sources.

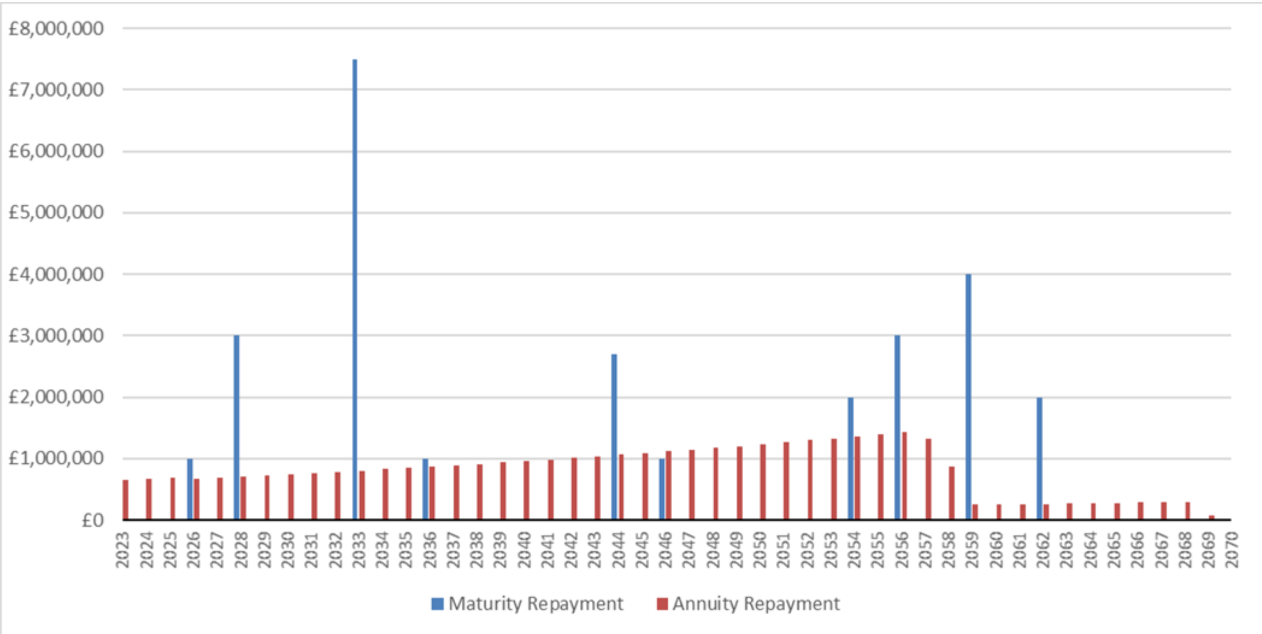
**Borrowing – Timing**

103. The general aim of this treasury management strategy is to minimise the costs of borrowing in both the short and longer term. In the short term it can consider avoiding new borrowing and using cash balances to finance new borrowing (internal borrowing). However, to minimise longer term costs it needs to borrow when rates are at lower levels. The timing of new borrowing is therefore important to minimise the overall costs to the Council.

104. The Council has previously sought to achieve near full financing of the Capital programme via external debt over recent years in order to take advantage of the historically low borrowing rates and avoid the risk of having to lock into high interest rates when it has no option but to borrow. For the last year, a higher level of internal borrowing was adopted to temporarily finance long life assets. Currently, with interest rates looking likely to increase further the Council is considering externalising some of the internal debt to lock in rates at lower levels.

**Debt Maturity**

105. The Graph below shows the profile of when debt (loans from the PWLB) become repayable. Blue lines indicate maturity loans and red lines indicate annuity loans.




106. The Council will need to carefully consider the structure and timing of any new borrowing to ensure debt does not exceed the CFR in the years ahead.

**Approved Sources of Long and Short-term Borrowing**

107. The following are the approved sources of long and short-term borrowings permitted by the council:

| On Balance Sheet | Fixed | Variable |
|---|---|---|
| PWLB | ● | ● |
| UK Municipal Bond Agency | ● | ● |

| | | |
|---|---|---|
| Local Authorities | ● | ● |
| Banks | ● | ● |
| Pension Funds | ● | ● |
| Insurance Companies | ● | ● |
| UK Infrastructure Bank | ● | ● |
| | | |
| Market (long-term) | ● | ● |
| Market (temporary) | ● | ● |
| Market (LOBOs) | ● | ● |
| Stock Issues | ● | ● |
| | | |
| Local Temporary | ● | ● |
| Local Bonds | ● | |
| Local Authority Bills | ● | ● |
| Overdraft | | ● |
| Negotiable Bonds | ● | ● |
| | | |
| Internal (capital receipts & revenue balances) | ● | ● |
| Commercial Paper | ● | |
| Medium Term Notes | ● | |
| Finance Leases | ● | ● |

**Summary**

108. No new external borrowing has been taken over the last 12 months but instead the council has been utilising internal borrowing to minimise interest costs.

109. The capital expenditure plans require no further new borrowing by the Council. The plans play a large part in the consideration as to when to borrow and the level of internal borrowing. The Council has taken advantage of other investment opportunities which have been providing higher returns than the cost of borrowing e.g., property funds. To date the Council has increased the level of internal funding in order to save on interest payments as the cost of these exceeds returns that can be achieved by investing surplus funds in the short term.

110. For the last few years, the cheapest borrowing has been internal borrowing by running down cash balances and foregoing interest earned at historically low rates. However, the Council may not have sufficient balances to temporarily finance all the capital expenditure in 2024/25 and may need to borrow before March 2025. In view of the overall forecast for long-term borrowing rates to remain static in the medium term, consideration has been given to weighing the short-term advantage of internal borrowing against the potential increase in long term costs if rates rise.

111. Where required, the use of PWLB variable rate loans for up to 10 years will still be considered as they can be repaid early without early redemption premiums. They can also be converted into longer dated fixed rate debt should it be considered prudent to do so.

112. The use of fixed rate market loans will also be considered should rates be below PWLB rates for the equivalent maturity period. The use of either PWLB maturity or annuity loans will be considered in order to minimise annual borrowing costs.

## ANNUAL INVESTMENT STRATEGY

### Investment Policy

113. The Department of Levelling Up, Housing and Communities (DLUHC - formerly the Ministry of Housing, Communities and Local Government (MHCLG)) and CIPFA have extended the meaning of 'investments' to include both financial and non-financial investments. This report deals solely with treasury (financial) investments, (as managed by the treasury management team). Non-financial investments, essentially the purchase of income yielding assets, are covered in the Capital Strategy.

114. The Council's investment policy has regard to the DLUHC's Guidance on Local Government Investments ("the Guidance"), the CIPFA Treasury Management in the Public Services Code of Practice and Cross Sectoral Guidance Notes 2021 ("the Code") and the CIPFA Treasury Management Guidance Notes 2021.

115. The Council has had various investment limits depending upon the credit rating e.g., £5m with any one institution with a minimum short-term rating of F+, and a long-term rating of A+ or above, supported by a red (6 month) rating by Link Group. The £5m limit generally represents a level of up to 25% of the investment portfolio with any one institution or group at any one time. It is also necessary, at times, to invest sums of this size in order to attract the larger institutions which have the higher credit ratings.

116. The guidance from the DLUHC and CIPFA places a high priority on the management of risk. This Council has adopted a prudent approach to managing risk and defines its risk appetite by the following means:

a) Minimum acceptable **credit criteria** are applied in order to generate a list of highly creditworthy counterparties. This also enables diversification and thus avoidance of concentration risk. The key ratings used to monitor counterparties are the short-term and long-term ratings.

b) **Other information:** ratings will not be the sole determinant of the quality of an institution; it is important to continually assess and monitor the financial sector on both a micro and macro basis and in relation to the economic and political environments in which institutions operate. The assessment will also take account of information that reflects the opinion of the markets. To achieve this consideration the Council will engage with its advisors to maintain a monitor on market pricing such as **"credit default swaps"** and overlay that information on top of the credit ratings.

c) **Other information sources** used will include the financial press, share price and other such information pertaining to the financial sector in order to establish the most robust scrutiny process on the suitability of potential investment counterparties.

d) This Council has defined the list of **types of investment instruments** that the treasury **management** team are authorised to use. There are two lists in Appendix 5 under the categories of 'specified' and 'non-specified' investments:

    **Specified investments** are those with a high level of credit quality and subject to a maturity limit of one year or have less than a year left to run to maturity if originally, they were classified as being non-specified investments solely due to the maturity period exceeding one year.

    **Non-specified investments** are those with less high credit quality, may be for periods in excess of one year, and/or **are** more complex instruments which require greater consideration by members and officers before being authorised for use.

e) **Lending limits**, (amounts and maturity), for each counterparty as set out in the **creditworthiness** policy below.

f) **Transaction limits** are set for each type of investment.

g) Investments will only be placed with counterparties from countries with a **specified minimum sovereign rating**.

h) This Council has engaged **external consultants** (Link Group), to provide expert advice on how to optimise an appropriate balance of security, liquidity, and yield, given the risk

**appetite** of the council in the context of the expected level of cash balances and need for liquidity throughout the year.

i) All investments will be denominated in **sterling**.

j) Consideration will be given to organisations Environmental, Social & Governance (ESG) credentials, although no scoring will be applied.

k) As a result of the change in accounting standards for 2023/24 under IFRS 9, this Authority will consider the implications of investment instruments which could result in an adverse movement in the value of the amount invested and resultant charges at the end of the year to the General Fund. (In November 2018, the MHCLG, concluded a consultation for a temporary override to allow English local authorities time to adjust their portfolio of all pooled investments by announcing a statutory override to delay implementation of IFRS 9 for five years ending 31.3.23. More recently, a further extension to the over-ride to 31.3.25 has been agreed by Government.

117. However, the Council will also pursue value for money in treasury management and will monitor the yield from investment income against appropriate benchmarks for investment performance. Regular monitoring of investment performance will be carried out during the year.

118. There are no changes in our risk management policy and the above criteria remain unchanged from last year.

**Creditworthiness Policy**

119. This Authority applies the creditworthiness service provided by the Link Group. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's, and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

1. "watches" and "outlooks" from credit rating agencies,
2. CDS spreads that may give early warning of changes in credit ratings,
3. sovereign ratings to select counterparties from only the most creditworthy countries.

120. This modelling approach combines credit ratings, and any assigned Watches and Outlooks, in a weighted scoring system which is then combined with an overlay of CDS spreads. The end-product of this is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will, therefore, use counterparties within the following durational bands:

- Yellow 5 years *
- Dark pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.25
- Light pink 5 years for Ultra-Short Dated Bond Funds with a credit score of 1.5
- Purple 2 years
- Blue 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange 1 year
- Red 6 months
- Green 100 days
- No colour not to be used

121. The Link creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

122. Typically, the minimum credit ratings criteria the Authority uses will be a short-term rating (Fitch or equivalents) of F1 and a long-term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances, consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

123. All credit ratings will be monitored monthly. The Council is alerted to changes to ratings of all three agencies through its use of the Link creditworthiness service.

- if a downgrade results in the counterparty / investment scheme no longer meeting the Authority's minimum criteria, its further use as a new investment will be withdrawn immediately.
- in addition to the use of credit ratings the Authority will be advised of information in movements in Credit Default Swap spreads against the iTraxx European Senior Financials benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link. Extreme market movements may result in downgrade of an institution or removal from the Authority's lending list.

124. Sole reliance will not be placed on the use of this external service. In addition, this Council will also use market data and market information, as well as information on any external support for banks to help support its decision-making process.

**Creditworthiness**

125. Significant levels of downgrades to Short and Long-Term credit ratings have not materialised since the crisis in March 2020. In the main, where they did change, any alterations were limited to Outlooks. Nonetheless, when setting minimum sovereign debt ratings, this Authority will not set a minimum rating for the UK.

**CDS prices**

126. Although bank CDS prices, (these are market indicators of credit risk), spiked upwards during the days of the Truss/Kwarteng government in the autumn of 2022, they have returned to more average levels since then. However, sentiment can easily shift, so it will remain important to undertake continual monitoring of all aspects of risk and return in the current circumstances. Link monitor CDS prices as part of their creditworthiness service to local authorities and the Authority has access to this information via its Link-provided Passport portal.

**Limits**

127. Due care will be taken to consider the exposure of the Council's total investment portfolio to non-specified investments, countries, groups, and sectors.

*a.* **Non-specified treasury management investment limit.** The Council has determined that it will limit the maximum total exposure of treasury management investments to non-specified treasury management investments as being 25% of the total treasury management investment portfolio.

*b.* **Country limit.** The Council has determined that it will only use approved counterparties from the UK and from countries with a **minimum sovereign credit rating of *AA-*** from Fitch *(or equivalent)*. The list of countries that qualify using this credit criteria as at the date of this report are shown in Appendix 6. This list will be added to, or deducted from, by officers should ratings change in accordance with this policy.

**Other limits**

128. In addition:

- no more than £10m will be placed with any non-UK country at any time,
- limits in place above will cumulatively apply to a group of companies/institutions,
- sector limits will be monitored regularly for appropriateness.

**Investment Strategy**

129. As at January 2024 the Council had cash balances amounting c£29.2m. The monies held are higher than would normally be expected and include monies that the Council is holding in respect of a number of grant schemes.

130. The Council's investment priorities will be security first, portfolio liquidity second, and then yield (return). The Council will aim to achieve the optimum return (yield) on its investments commensurate with proper levels of security and liquidity and with the Council's risk appetite.

131. The Chief Finance Officer has the authority to amend the limits on a daily basis, if necessary, to ensure that monies can be placed with appropriate institutions. The use of Money Market

funds is anticipated, the Council is setup on a portal to allow access to a diversified range of money market funds from different providers.

132. The effects of the pandemic and conflicts continue to impact on countries around the world and in turn on credit ratings. The Council follows the Credit ratings of Link Group, and the ratings now enable the Council to invest £5m with any one institution with a minimum short-term rating of F (rather than F+), and a long-term rating of A+ and above (Unchanged), supported by a red (6 month) rating.

133. In the current economic climate, it is considered appropriate to maintain a degree of liquidity to cover cash flow needs but to also consider "laddering" investments for periods up to 12 months with high credit rated financial institutions, whilst investment rates remain elevated, as well as wider range fund options. The Council is in the position to ensure that its cash balances are spread across numerous counterparties.

134. **In-house funds.** Investments will be made with reference to the core balance and cash flow requirements and the outlook for short-term interest rates (i.e., rates for investments up to 12 months). Greater returns are usually **obtainable** by investing for longer periods. The current shape of the yield curve suggests that is the case at present, but there is the prospect of Bank Rate having peaked in the second half of 2023 and possibly reducing as early as the second half of 2024 so an agile investment strategy would be appropriate to optimise returns.

135. Accordingly, while most cash balances are required in order to manage the ups and downs of cash flow, where cash sums can be identified that could be invested for longer periods, the value to be obtained from longer-term investments will be carefully assessed.

**Investment returns expectations.**

136. The current forecast shown in paragraph 70, includes a forecast for Bank Rate to have peaked at 5.25%.

137. The suggested budgeted investment earnings rates for returns on investments placed for periods up to about three months during each financial year are as follows: -

| Average earnings in each year | |
|---|---|
| 2023/24 (residual) | 5.30% |
| 2024/25 | 4.55% |
| 2025/26 | 3.10% |
| 2026/27 | 3.00% |
| 2027/28 | 3.25% |
| Years 6 to 10 | 3.25% |
| Years 10+ | 3.25% |

138. As there are so many variables at this time, caution must be exercised in respect of all interest rate forecasts.

139. For cash flow generated balances, the Council will seek to utilise its business reserve instant access and notice accounts, Money Market Funds, and short-dated deposits, (overnight to 100 days), in order to benefit from the compounding of interest.

**Investment treasury indicator and limit**

140. For total principal funds invested for greater than 365 days, these limits are set with regard to the Council's liquidity requirements and to reduce the need for early sale of an investment and are based on the availability of funds after each year-end.

141. The Council is asked to approve the following treasury indicator and limit:

| Upper limit for principal sums invested for longer than 365 days | | | |
|---|---|---|---|
| **£m** | **2024/25** | **2025/26** | **2026/27** |
| Principal sums invested for longer than 365 days | £5m | £5m | £5m |
| Current investments as at 31/12/23 in excess of 1 year maturing in each year | £5m | £5m | £5m |

## Investment Strategy – Property Fund

142. It was agreed in February 2017 that the option for diversification of some of the investments into a property fund be undertaken with CCLA in the sum of £2m. The investment being in respect of the Council's reserves that are not required for a period of at least 5 years in order that any fall in values and entry costs into such funds can be covered. The £2m was invested in April 2017 and the performance is detailed below:

**Table 6: CCLA – LA's Property Prices and Dividend yields**

| End of | Sept 23 | June 23 | Mar-23 | Mar-22 | Mar-21 | Mar-20 | Mar-19 |
|---|---|---|---|---|---|---|---|
| Offer Price p | 303.70 | 307.30 | 307.73 | 368.46 | 313.45 | 315.7 | 327.4 |
| Net Asset Value p | 284.50 | 287.87 | 288.27 | 345.17 | 293.63 | 295.74 | 306.7 |
| Bid Price p | 280.09 | 283.41 | 283.80 | 339.82 | 289.08 | 291.15 | 301.95 |
| Dividend* on XD Date p | 3.74 | 3.35 | 3.09 | 2.7875 | 2.9797 | 3.25 | 3.31 |
| Dividend* - Last 12 Months p | 13.27 | 12.79 | 12.29 | 11.22 | 12.63 | 13.06 | 13.08 |
| Dividend Yield on NAV % | 4.66 | 4.44 | 4.26 | 3.13 | 4.3 | 4.41 | 4.26 |

143. The dividend yield is currently around 4.7% p.a. on the net asset value. Dividends for the first 2 quarters of 2023/24 amount to £46,160 (£39,811 at the same point last year). Full year dividends for 2023/24 are estimated at around £86,400 and a similar return is anticipated for 2024/25.

**Table 7: CCLA - Property Fund Capital Value**

| Units (651,063) | Sep-23 | Jun-23 | Mar-23 | Mar-22 | Mar-21 | Mar-20 | Mar-19 |
|---|---|---|---|---|---|---|---|
| Mid-Market Price(£) | 1,852,274 | 1,882,874 | 1,876,819 | 2,247,274 | 1,911,716 | 1,925,454 | 1,996,810 |
| Bid Price (£) | 1,823,562 | 1,845,178 | 1,847,717 | 2,212,442 | 1,882,093 | 1,895,570 | 1,965,885 |

144. The Capital value (Net market Value) has decreased by 7.2% between April 2020 and September 2023 and is now below the original investment.

## Diversified Income Fund

145. It was agreed in February 2019 that a sum of £3m would be made available for further diversification of the Council's investments. £1m was invested on 26 July 2019 and a further £2m investment was made on 24 September 2019 into the CCLA Diversified Income Fund. Anticipated returns were around 3% with the added advantage of much higher liquidity than the property fund.

146. The market value of the initial investment was £3,012,479 as at the end of December 2019. In March 2020 the market value had fallen to £2,620,089, this has seen a recovery with a market value of £2,824,439 on 29 December 2023 (6.2% below the initial investment value). Dividend yield on price was 3.25% for December 2023 (3.0% March 2023). Dividends payable for the first 2 quarters of 2023/24 amount to £41,073 (£44,402 for the same period last year). It should be remembered that this is a long-term investment and prices can go up and down.

## Investment Performance / Risk Benchmarking

147. This Authority will use an investment benchmark to assess the investment performance of its investment portfolio of overnight, 7 day, 1, 3, 6 or 12 month compounded / SONIA.

## End of Year Investment Report

148. At the end of the financial year, the Council will report on its investment activity as part of its Annual Treasury Report.

## Regeneration and Economic Development - Income Generation

149. The Council has remained keen to pursue capital schemes that also generate income. Substantial investments in housing and energy projects will necessitate new borrowing. The levels of new borrowing that the Council can afford to take on board will be dependent upon the individual proposals and credit worthiness of the counterparties involved.

150. The additional risks that the Council is taking on need to be considered in the context of the totality of risk that the Council faces e.g., external claims, rates revaluation, robustness of income streams, economic downturns, etc. Where there is more risk and volatility in income streams, the Council will need to ensure that it maintains sufficient reserves to ensure the Council's ability to deliver key

services is not jeopardised.

**Policy on Use of External Service Providers**

151. The Council uses Link Group, Treasury solutions as its external treasury management advisors. There is currently value in employing external providers of treasury management services in order to acquire access to credit worthiness information and specialist advice.

**Training**

152. The CIPFA Code requires the responsible officer (Chief Financial Officer) to ensure that members with responsibility for treasury management receive adequate training in treasury management. This especially applies to members responsible for scrutiny. In terms of treasury management in general, training has been undertaken by members on an annual basis to date.

153. Furthermore, the Code state that they expect "all organisations to have a formal and comprehensive knowledge and skills or training policy for the effective acquisition and retention of treasury management knowledge and skills for those responsible for management, delivery, governance, and decision making.

154. As a minimum, authorities should carry out the following to monitor and review knowledge and skills:

- Record attendance at training and ensure action is taken where poor attendance is identified.
- Prepare tailored learning plans for treasury management officers and key members.
- Require treasury management officers and key members to undertake self- assessment against the required competencies.
- Have regular communication with officers and key members, encouraging them to highlight training needs on an ongoing basis.

155. Treasury Management Training was offered to all members on 11th January 2023 with further training arranged, as required.

156. The training needs of treasury management officers are periodically reviewed.

157. A formal record of the training received by officers and members central to the Treasury function is maintained by the Deputy Chief Finance Officer.

**MiFID II (Markets in Financial Instruments Directive)**

158. In brief, this directive requires the Council to distinguish itself as either a retail or professional client. In order to qualify for professional status, the Council is required to show that it has more than £10m in investments, invests regularly (more than 10 times a quarter), as well as having appropriately trained and experienced staff.

159. To date only two counterparties have required us to complete the forms in order to maintain the existing professional status. The directive became law on 1 January 2018.

160. The two parties to date are Link Group and CCLA. A schedule of such counterparties will be maintained, as per the requirements of the Code, should the list expand further.

**Scheme of Delegation**

161. Please see Appendix 9.

**Role of the Section 151 Officer**

162. Please see Appendix 10.

APPENDIX 1

# Minimum Revenue Provision – An Introduction

### What is a Minimum Revenue Provision?

Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g., buildings, vehicles, machinery etc. It would be impractical to charge the entirety of such expenditure to revenue in the year in which it was incurred therefore such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision, which was previously determined under Regulation, and will in future be determined under Guidance.

### Statutory duty

Under Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, where the Authority has financed capital expenditure by borrowing it is required to make a provision each year through a revenue charge (MRP).

The Authority is required to calculate a prudent provision of MRP which ensures that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The MRP Guidance (2018) gives four ready-made options for calculating MRP, but the Authority can use any other reasonable basis that it can justify as prudent.

The MRP policy statement requires full Council approval in advance of each financial year.

There is no requirement to charge MRP where the Capital Financing Requirement is nil or negative at the end of the preceding financial year.

### Government Guidance

Along with the above duty, the Government issued guidance which came into force on 31st March 2008 which requires that a Statement on the Council's policy for its annual MRP should be submitted to the full Council for approval before the start of the financial year to which the provision will relate.

The Council is legally obliged to "have regard" to the guidance, which is intended to enable a more flexible approach to assessing the amount of annual provision than was required under the previous statutory requirements. The guidance offers four main options under which MRP could be made, with an overriding recommendation that the Council should make prudent provision to redeem its debt liability over a period which is reasonably commensurate with that over which the capital expenditure is estimated to provide benefits. The requirement to 'have regard' to the guidance therefore means that: -

Although four main options are recommended in the guidance, there is no intention to be prescriptive by making these the only methods of charge under which a local authority may consider its MRP to be prudent.

It is the responsibility of each authority to decide upon the most appropriate method of making a prudent provision, after having had regard to the guidance.

### Option 1: Regulatory Method

Under the previous MRP regulations, MRP was set at a uniform rate of 4% of the adjusted CFR (i.e., adjusted for "Adjustment A") on a reducing balance method (which in effect meant that MRP charges would stretch into infinity). This historic approach must continue for all capital expenditure incurred in years before the start of this new approach. It may also be used for new capital expenditure up to the amount which is deemed to be supported through the Supported Capital Expenditure (SCE) annual allocation.

### Option 2: Capital Financing Requirement Method

This is a variation on option 1 which is based upon a charge of 4% of the aggregate CFR without any adjustment for Adjustment A, or certain other factors which were brought into account under the previous statutory MRP calculation. The CFR is the measure of an authority's outstanding debt liability as depicted by their balance sheet.

**Option 3: Asset Life Method.**

This method may be applied to most new capital expenditure, including where desired that which may alternatively continue to be treated under options 1 or 2.

Under this option, it is intended that MRP should be spread over the estimated useful life of either an asset created, or other purpose of the expenditure. There are two useful advantages of this option: -

- Longer life assets e.g., freehold land can be charged over a longer period than would arise under options 1 and 2.
- No MRP charges need to be made until the financial year after that in which an item of capital expenditure is fully incurred and, in the case of a new asset, comes into service use (this is often referred to as being an 'MRP holiday'). This is not available under options 1 and 2.

There are two methods of calculating charges under option 3:

- equal instalment method – equal annual instalments,
- annuity method – annual payments gradually increase during the life of the asset.

**Option 4: Depreciation Method**

Under this option, MRP charges are to be linked to the useful life of each type of asset using the standard accounting rules for depreciation (but with some exceptions) i.e., this is a more complex approach than option 3.

The same conditions apply regarding the date of completion of the new expenditure as apply under option 3.

**Minimum Revenue Provision Policy Statement 2024/25**

Under Regulation 27 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003, where the Authority has financed capital expenditure by borrowing it is required to make a provision each year through a revenue charge (MRP).

Regulation 28 of the Local Authorities (Capital Finance and Accounting) (England) (Amendment) regulations 2008 require the Authority to calculate a prudent provision of MRP whilst having regard to the current MRP Guidance (2018). The broad aim of prudent provision is to ensure that the outstanding debt liability is repaid over a period that is reasonably commensurate with that over which the capital expenditure provides benefits. The Guidance gives four ready-made options for calculating MRP, but the Authority can use any other reasonable basis that it can justify as prudent.

The MRP policy statement requires full Council approval in advance of each financial year.

It is recommended that Council approves the following MRP Policy Statement.

- Supported borrowing incurred before 1st April 2008 will apply the Asset Life Method using an annuity calculation over 50 years.

- Unsupported borrowing will be subject to MRP using the Asset Life Method, which will be charged over a period which is reasonably commensurate with the estimated useful life of the assets. An annuity method will be applied for the MRP calculation.

- The interest rate applied to the annuity calculations will reflect the market conditions at the time. For the 2024/25 financial year the interest rate used will be average PWLB rate for the year.

- MRP will commence in the financial year following the one in which the expenditure was incurred, or in the year after the asset becomes operational.

- MRP in respect of unsupported borrowing taken to meet expenditure, which is treated as capital expenditure by virtue of either a capitalisation direction or regulations, will be determined in accordance with the asset life method as recommended by the MRP guidance.

- MRP in respect of assets acquired under PFI or Finance Leases will be charged at a rate equal to the principal element of the annual lease rental for the year in question.
- MRP Overpayments - The MRP Guidance allows that any charges made in excess of the statutory MRP, i.e., voluntary revenue provision (VRP) or overpayments, can be reclaimed in later years if deemed necessary or prudent. In order for these sums to be reclaimed for use in the budget, this policy must disclose the cumulative overpayment made each year. The VRP overpayments up to 31st March 2023 are £0.
- On an annual basis the Section 151 Officer shall review the level of MRP to be charged, to determine if this is at a level which is considered prudent based on the Authority's circumstances at that time, taking into account medium / long term financial plans, current budgetary pressures, current and future capital expenditure plans. Dependant on this review the Section 151 officer will adjust the annual MRP charge by making VRP or reclaiming previous VRP. The amount of MRP charged *shall not be less than zero in any financial year.*

## APPENDIX 2 - Interest Rate Forecasts

Link Group Interest rate forecast – March 2024 – March 2027

| Link Group Interest Rate View 08.01.24 | Mar-24 | Jun-24 | Sep-24 | Dec-24 | Mar-25 | Jun-25 | Sep-25 | Dec-25 | Mar-26 | Jun-26 | Sep-26 | Dec-26 | Mar-27 |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| BANK RATE | 5.25 | 5.25 | 4.75 | 4.25 | 3.75 | 3.25 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 3 month ave earnings | 5.30 | 5.30 | 4.80 | 4.30 | 3.80 | 3.30 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 | 3.00 |
| 6 month ave earnings | 5.20 | 5.10 | 4.60 | 4.10 | 3.70 | 3.30 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 |
| 12 month ave earnings | 5.00 | 4.90 | 4.40 | 3.90 | 3.60 | 3.20 | 3.10 | 3.10 | 3.10 | 3.10 | 3.10 | 3.20 | 3.20 |
| 5 yr PWLB | 4.50 | 4.40 | 4.30 | 4.20 | 4.10 | 4.00 | 3.80 | 3.70 | 3.60 | 3.60 | 3.50 | 3.50 | 3.50 |
| 10 yr PWLB | 4.70 | 4.50 | 4.40 | 4.30 | 4.20 | 4.10 | 4.00 | 3.90 | 3.80 | 3.70 | 3.70 | 3.70 | 3.70 |
| 25 yr PWLB | 5.20 | 5.10 | 4.90 | 4.80 | 4.60 | 4.40 | 4.30 | 4.20 | 4.20 | 4.10 | 4.10 | 4.10 | 4.10 |
| 50 yr PWLB | 5.00 | 4.90 | 4.70 | 4.60 | 4.40 | 4.20 | 4.10 | 4.00 | 4.00 | 3.90 | 3.90 | 3.90 | 3.90 |

**Note: PWLB forecasts are based on PWLB certainty rates.**

## APPENDIX 3 - Economic Review (by Link Group)

### ECONOMIC BACKGROUND

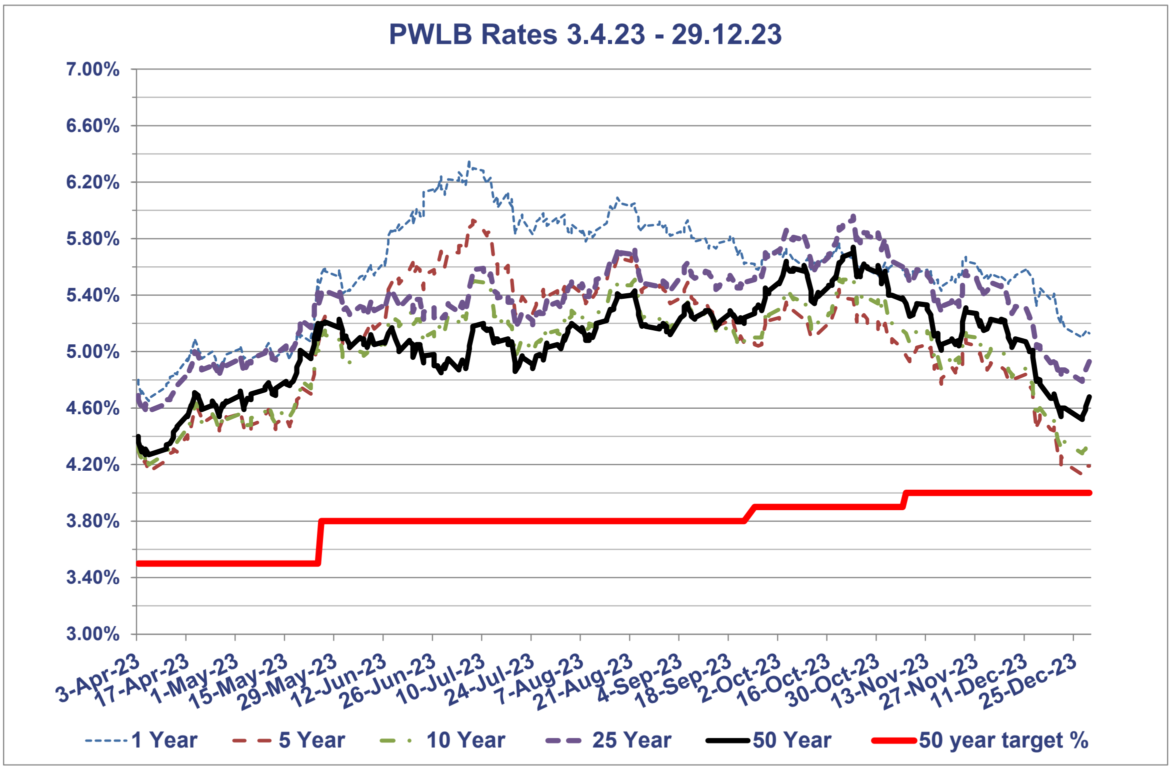
- The third quarter of 2023/24 saw:
  - A 0.3% m/m decline in real GDP in October, potentially partly due to unseasonably wet weather, but also due to the ongoing drag from higher interest rates. Growth for the second quarter, ending 30th September, was revised downwards to -0.1% and growth on an annual basis was also revised downwards, to 0.3%.
  - A sharp fall in wage growth, with the headline 3myy rate declining from 8.0% in September to 7.2% in October, although the ONS "experimental" rate of unemployment has remained low at 4.2%.
  - CPI inflation continuing on its downward trajectory, from 8.7% in April to 4.6% in October, then again to 3.9% in November.
  - Core CPI inflation decreasing from April and May's 31 years' high of 7.1% to 5.1% in November, the lowest rate since January 2022.
  - The Bank of England holding Bank Rate at 5.25% in November and December.
  - A steady fall in 10-year gilt yields as investors revised their interest rate expectations lower.
- The revision of GDP data in Q2 to a 0.1% q/q fall may mean the mildest of mild recessions has begun. Indeed, real GDP in October fell 0.3% m/m which does suggest that the economy may stagnate again in Q3. The weakness in October may partly be due to the unseasonably wet weather. That said, as the weakness was broad based it may also be the case that the ongoing drag from higher interest rates is more than offsetting any boost from the rise in real wages.
- However, the rise in the flash composite activity Purchasing Managers Index, from 50.7 in November to 51.7 in December, did increase the chances of the economy avoiding a contraction in Q3. The improvement was entirely driven by the increase in the services activity balance from 50.9 to 52.7. (Scores above 50 points to expansion in the economy, although only tepid in this instance.) The press release noted that this was primarily driven by a revival in consumer demand in the technological and financial services sectors. This chimes with the further improvement in the GfK measure of consumer confidence in December, from -24 to -22. The services PMI is now consistent with non-retail services output growing by 0.5% q/q in Q3, but this is in stark contrast to the manufacturing sector where the output balance slumped from 49.2 to 45.9 and, at face value, the output balance is consistent with a 1.5% q/q fall in manufacturing output in Q3.
- The 0.3% m/m fall in retail sales volumes in October means that after contracting by 1.0% q/q (which was downwardly revised from -0.8% q/q) in Q2, retail activity remained weak at the start of Q3. That suggests higher interest rates are taking a bigger toll on real consumer spending.
- Higher interest rates have filtered through the financial channels and weakened the housing market but, overall, it remains surprisingly resilient with the Halifax house price index recently pointing to a 1.7% year on year increase whilst Nationwide's December data pointed to a -1.8% year on year decrease. However, the full weakness in real consumer spending and real business investment has yet to come as currently it is estimated that around two thirds to a half of the impact of higher interest rates on household interest payments has yet to be felt.
- Overall, we expect real GDP growth to remain subdued throughout 2024 as the drag from higher interest rates is protracted but a fading of the cost-of-living crisis and interest rate cuts in the second half of 2024 will support a recovery in GDP growth in 2025.

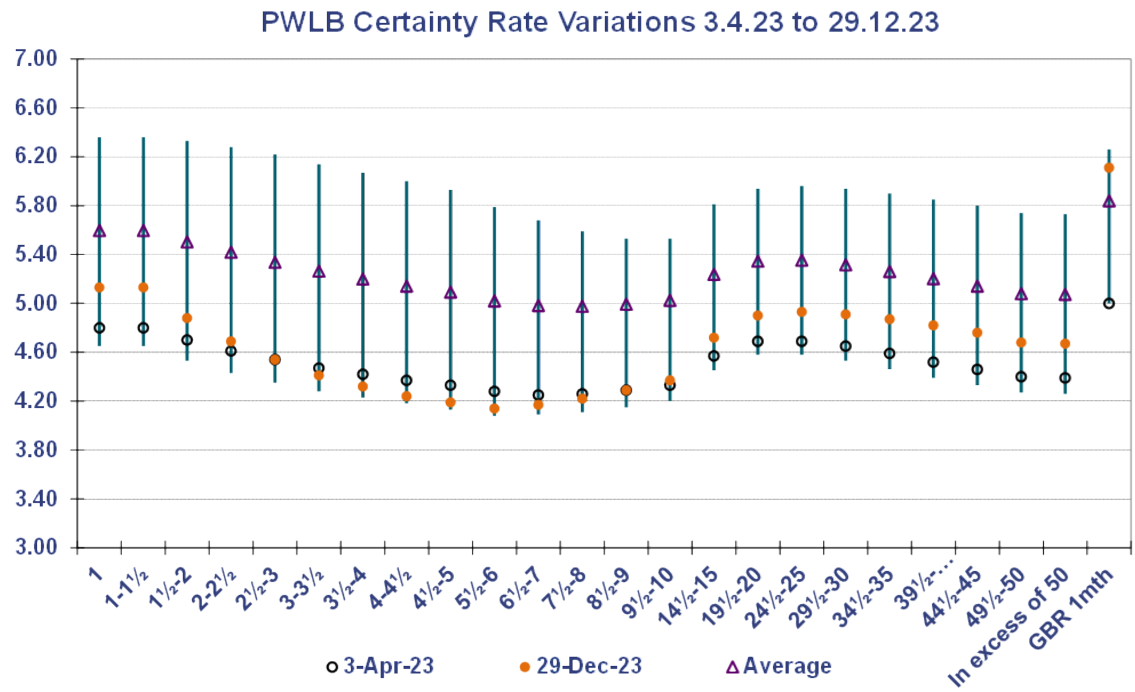
- The labour market remains tight by historical standards, but the sharp fall in wage growth seen in October will reinforce the growing belief in markets that interest rates will be cut mid-2024. Wage growth eased in October much faster than the consensus expected. Total earnings fell by 1.6% m/m, which meant the headline 3myy rate eased from 8.0% in September to 7.2% in October. This news will be welcomed by the Bank of England. Indeed, the timelier three-month annualised rate of average earnings growth fell from +2.4% to -1.2%. Excluding bonuses, it fell from 5.3% to 2.0%. Furthermore, one of the Bank's key barometers of inflation persistence, regular private sector pay growth, dropped from 7.9% 3myy to 7.3%, which leaves it comfortably on track to fall to 7.2% by December, as predicted by the Bank in November.
- The fall in wage growth occurred despite labour demand being stronger in October than expected. The three-month change in employment eased only a touch from +52,000 in September to +50,000 in October. But resilient labour demand was offset by a further 63,000 rise in the supply of workers in the three months to October. That meant labour supply exceeded its pre-pandemic level for the first time, and the unemployment rate remained at 4.2% in October. In the three months to November, the number of job vacancies fell for the 17th month in a row, from around 959,000 in October to around 949,000. That has reduced the vacancy to unemployment ratio as demand for labour eases relative to supply, which may support a further easing in wage growth in the coming months.
- CPI inflation fell from 6.7% in September to 4.6% in October, and then again to 3.9% in November. Both these falls were bigger than expected and there are clear signs of easing in domestic inflationary pressures. The fall in core CPI inflation from 5.7% to 5.1% in November was bigger than expected (consensus forecast 5.6%). That is the lowest rate since January 2022. Some of the decline in core inflation was due to the global influence of core goods inflation, which slowed from 4.3% to 3.3%. But some of it was due to services inflation falling from 6.6% to 6.3%. The Bank views the latter as a key barometer of the persistence of inflation and it came in further below the Bank's forecast of 6.9% in its November Monetary Policy Report. This will give the Bank more confidence that services inflation is now on a firmly downward path.
- The Bank of England sprung no surprises with its December monetary policy committee (MPC) meeting, leaving interest rates at 5.25% for the third time in a row and pushing back against the prospect of near-term interest rate cuts. The Bank continued to sound hawkish, with the MPC maintaining its tightening bias saying that "further tightening in monetary policy would be required if there were evidence of more persistent inflationary pressures." And it stuck to the familiar script, saying that policy will be "sufficiently restrictive for sufficiently long" and that "monetary policy is likely to need to be restrictive for an extended period of time." In other words, the message is that the MPC is not yet willing to endorse investors' expectations that rates will be cut as soon as May 2024.
- Looking ahead, our colleagues at Capital Economics forecast that the recent downward trends in CPI and core inflation will stall over the next few months before starting to decline more decisively again in February. That explains why we think the Bank of England will not feel comfortable cutting interest rates until H2 2024.
- The fall in UK market interest rate expectations in December has driven most of the decline in 10-year gilt yields, which have fallen in line with 10-year US Treasury and euro-zone yields. 10-year gilt yields have fallen from 4.68% in October 2023 to around 3.70% in early January, with further declines likely if the falling inflation story is maintained.
- Investors' growing expectations that the Fed will cut interest rates soon has led to an improvement in risk sentiment, which has boosted the pound and other risky assets. In addition, the rise in the pound, from $1.21 in November to $1.27 now, has also been supported by the recent relative decline in UK wholesale gas prices.

- The further fall in 10-year gilt yields in December has supported the recent rise in the FTSE 100. That said, the index remains 5% below its record high in February 2023. This modest rise in equities appears to have been mostly driven by strong performances in the industrials and rate-sensitive technology sectors. But UK equities have continued to underperform US and euro-zone equities. The FTSE 100 has risen by 2.2% in December, while the S&P 500 has risen by 3.8%. This is partly due to lower energy prices, which have been a relatively bigger drag on the FTSE 100, due to the index's high concentration of energy companies.

In the chart below, the rise in gilt yields across the curve in the first half of 2023/24, and therein PWLB rates, is clear to see, prior to the end of year rally based on a mix of supportive domestic and international factors.

**PWLB RATES 3.4.23 - 29.12.23**



**HIGH/LOW/AVERAGE PWLB RATES FOR 3.4.23 – 29.12.23**

| | 1 Year | 5 Year | 10 Year | 25 Year | 50 Year |
|---|---|---|---|---|---|
| **Low** | 4.65% | 4.13% | 4.20% | 4.58% | 4.27% |
| **Date** | 06/04/2023 | 27/12/2023 | 06/04/2023 | 06/04/2023 | 05/04/2023 |
| **High** | 6.36% | 5.93% | 5.53% | 5.96% | 5.74% |
| **Date** | 06/07/2023 | 07/07/2023 | 23/10/2023 | 23/10/2023 | 23/10/2023 |
| **Average** | 5.60% | 5.09% | 5.03% | 5.35% | 5.08% |
| **Spread** | 1.71% | 1.80% | 1.33% | 1.38% | 1.47% |

**MPC meetings 2nd November and 14th December 2023**

- On 2nd November, the Bank of England's Monetary Policy Committee (MPC) voted to keep Bank Rate on hold at 5.25%, and on 14th December reiterated that view. Both increases reflected a split vote, the latter by 6 votes to 3, with the minority grouping voting for an increase of 0.25% as concerns about "sticky" inflation remained in place.
- Nonetheless, with UK CPI inflation now at 3.9%, and core inflating beginning to moderate (5.1%), markets are voicing a view that rate cuts should begin in Q1 2024/25, some way ahead of the indications from MPC members. Of course, the data will be the ultimate determinant, so upcoming publications of employment, wages and inflation numbers will be of particular importance, and on-going volatility in Bank Rate expectations and the gilt yield curve can be expected.
- In addition, what happens outside of the UK is also critical to movement in gilt yields. The US FOMC has kept short-term rates in the range of 5.25%-5.50%, whilst the ECB has moved its Deposit rate to a probable peak of 4%. Markets currently expect both central banks to start cutting rates in 2024.

## APPENDIX 4 - Prudential Indicators

The Council's Capital expenditure plans are the key driver of treasury management activity. The output of the Capital expenditure plans (detailed in the budget) is reflected in the prudential indicators below.

| **TREASURY MANAGEMENT PRUDENTIAL INDICATORS** | **2022/23** | **2023/24** | **2024/25** | **2025/26** | **2026/27** |
|---|---|---|---|---|---|
| | £'000 | £'000 | £'000 | £'000 | £'000 |
| **Authorised Limit for external debt** | | | | | |
| borrowing | 110,000 | 135,000 | 135,000 | 135,000 | 135,000 |
| other long-term liabilities | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| **TOTAL** | 115,000 | 140,000 | 140,000 | 140,000 | 140,000 |
| **Operational Boundary for external debt** | | | | | |
| borrowing | 105,000 | 130,000 | 130,000 | 130,000 | 130,000 |
| other long-term liabilities | 5,000 | 5,000 | 5,000 | 5,000 | 5,000 |
| **TOTAL** | 110,000 | 135,000 | 135,000 | 135,000 | 135,000 |

| **Interest Rate Exposures** | **2023/24 Upper** | **2024/25 Upper** | **2025/26 Upper** |
|---|---|---|---|
| Limits on fixed interest rates based on **net** debt | 100% | 100% | 100% |
| Limits on variable interest rates based on **net** debt | 100% | 100% | 100% |
| Limits on fixed interest rates: | | | |
| · Debt only | 100% | 100% | 100% |
| · Investments only | 100% | 100% | 100% |
| Limits on variable interest rates | | | |
| · Debt only | 30% | 30% | 30% |
| · Investments only | 100% | 100% | 100% |

| **Maturity Structure of fixed interest rate borrowing 2024/25** | **Lower** | **Upper** |
|---|---|---|
| Under 12 Months | 0% | 100% |
| 12 months to 2 years | 0% | 100% |
| 2 years to 5 years | 0% | 100% |
| 5 years to 10 years | 0% | 100% |
| 10 years to 20 years | 0% | 100% |
| 20 years to 30 years | 0% | 100% |
| 30 years to 40 years | 0% | 100% |
| 40 years to 50 years | 0% | 100% |

| **Maturity Structure of variable interest rate borrowing 2024/25** | **Lower** | **Upper** |
|---|---|---|
| Under 12 Months | 0% | 30% |
| 12 months to 2 years | 0% | 30% |
| 2 years to 5 years | 0% | 30% |
| 5 years to 10 years | 0% | 30% |
| 10 years to 20 years | 0% | 10% |
| 20 years to 30 years | 0% | 10% |
| 30 years to 40 years | 0% | 10% |
| 40 years to 50 years | 0% | 10% |

**Affordability Prudential Indicator - Ratio of financing costs to net revenue stream.**

This indicator assesses the affordability of the capital investment plans. It provides an indication of the impact of the capital investment plans on the Council's overall finances. This indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

| Prudential Indicator: Financing Cost to Net Revenue Stream | 2021/22 Actual | 2022/23 Estimate | 2023/24 Estimate | 2024/25 Estimate | 2025/26 Estimate |
|---|---|---|---|---|---|
| **Financing Costs** | £'000 | £'000 | £'000 | £'000 | £'000 |
| 1. Interest Charged to General Fund | 1,862 | 2,435 | 1,817 | 1,817 | 1,817 |
| 2. Interest Payable under Finance Leases and any other long-term liabilities | - | - | - | - | - |
| 3. Gains and losses on the repurchase or early settlement of borrowing credited or charged to the amount met from government grants and local taxpayers | - | - | - | - | - |
| 4. Interest and Investment Income | (540) | (808) | (824) | (618) | (618) |
| 5. Amounts payable or receivable in respect of financial derivatives | - | - | - | - | - |
| 6. Minimum Revenue Provision (MRP) / Voluntary Revenue Provision (VRP) | 870 | 904 | 966 | 1,021 | 1,125 |
| 7. Depreciation/Impairment that are charged to the amount to be met from government grants and local taxpayers | - | - | - | - | - |
| **Total** | 1,591 | 2,009 | 1,483 | 1,538 | 1,642 |
| **Net Revenue Stream** Amount to be met from government grants and local taxpayers | 14,743 | 15,752 | 14,829 | 14,404 | 16,122 |
| **Ratio** **Financing Cost to Net Revenue Stream** | **11%** | **13%** | **10%** | **11%** | **10%** |

This prudential indicator shows that the ratio of financing costs to the net revenue stream is increasing. This is not unexpected given that the Council has had an income generation strategy that has resulted in increased Capital expenditure over the period 2017/18 to 2021/22 and that the Council agreed a programme for over £54m of Capital expenditure over the period 2020/21 to 2023/24 - thus increasing borrowing costs. The above ratio does not take into account the income is being generated from some of the initiatives and commercial property acquisitions as these are not treated as investment income.

**Other Prudential Indicators**

Gearing is the amount of debt – in proportion to equity capital – that a company uses to fund its operations. An entity that possesses a high gearing ratio shows a high debt to equity ratio, which potentially increases the risk of financial failure of the business. The Council's current gearing ratio is forecast to be 34% for 23/24, forecast to drop to 29% in 26/27. This indicates that we have more than three times the value in assets to cover our long-term liabilities.

Internal Borrowing and Gearing ratios for the authority are included in the Capital Strategy.

**APPENDIX 5 - Specified and Non-Specified Investments**

**Specified Investments:**

The idea of specified investments is to identify investments offering high security and high liquidity. All these investments should be in sterling and with a maturity of up to a maximum of one year.

**Schedule A**

| | Security / Minimum Credit Rating | Maximum Maturity Period |
|---|---|---|
| Local authorities | N/A | 1 year |
| DMADF – UK Government | N/A | 1 year |
| Money Market Funds (CNAV, LVAV,VNAV) | AAA | Liquid |
| Term deposits with banks and building societies | Blue<br>Orange<br>Red<br>Green<br>No Colour | Up to 1 year<br>Up to 1 year<br>Up to 6 months<br>Up to 3 months<br>Not for use |
| Certificates of deposits (CDs) issued by credit rated deposit takers (banks and building societies) | Blue<br>Orange<br>Red<br>Green<br>No Colour | Up to 1 year<br>Up to 1 year<br>Up to 6 months<br>Up to 3 months<br>Not for use |
| UK Government Gilts | UK sovereign rating | 12 months |
| UK Government Treasury Bills | UK sovereign rating | 12 months |

**Non-Specified Investments**

These are any investments which do not meet the specified investment criteria.

The aim is to ensure that proper procedures are in place for undertaking risk assessments of investments made for longer periods or with bodies which do not have a “high” credit rating. As far as this Council is concerned the risks are in relation to the value of the investments, which may rise, or fall, rather than deficient credit rating.

There is no intention to invest in Non-Specified Investments, other than those Property Funds where there are no Capital accounting implications, without taking specialist advice first. The limits on Investments in Property Funds will be agreed as part of this Treasury Management Strategy and Investment Policy. For clarity, any increase in the level of the investment would need Council approval.

**Schedule B**

| Investment | Security / Minimum credit rating | (A) Why use it?<br>(B) Associated risks |
|---|---|---|
| Property Funds | *The use of these instruments can be deemed capital expenditure, and as such will be an application (spending) of capital resources. This Authority will check on the status of any fund it may consider using. Appropriate due diligence will also be undertaken before investment of this type is undertaken. These are longer term investments and will extend beyond 365 days (expected to be invested for 5 years or more)* | |
| UK Government Gilts with maturities in excess of 1-year Custodial arrangement required prior to purchase | Government backed | (A) Why use it?<br>(i) Excellent credit quality.<br>(ii) Very liquid.<br>(iii) if held to maturity, known yield (rate of return) per annum – aids forward planning.<br>(iv) If traded, potential for capital gain through appreciation in value (i.e., sold before maturity)<br>(v) No currency risk.<br>(B) Associated risks<br>(i) 'Market or interest rate risk': Yield subject to movement during life of sovereign bond which could negatively impact on price of the bond i.e., potential for capital loss. |

## APPENDIX 6 - Approved Countries for Investments

This list is based on those countries which have sovereign ratings of AA- or higher, (we show the lowest rating from Fitch, Moody's, and S&P) and also, (except - at the time of writing - for Hong Kong and Luxembourg), have banks operating in sterling markets which have credit ratings of green or above in the Link creditworthiness service.

***Based on lowest available rating***

**AAA**

- Australia
- Denmark
- Germany
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

**AA+**

- Canada
- Finland
- U.S.A.

**AA**

- Abu Dhabi (UAE)

**AA-**

- Belgium
- France
- Qatar
- **U.K.**

**APPENDIX 7 - Treasury Management Policy Statement**

The Council defines the policies and objectives of its treasury management activities as:

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

This Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management."

## APPENDIX 8 - Key Principles and Clauses formally adopted.

The Code identifies three key principles:

**Key Principle 1**

Public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities.

**Key Principle 2**

Their policies and practices should make clear that the effective management and control of risk are the prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy, including any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and portfolio liquidity when investing treasury management funds.

**Key Principle 3**

They should acknowledge that the pursuit of value for money in treasury management and the use of suitable performance measures, are valid and important tools for responsible organisations to employ in support of their business and service objectives; and that within the context of effective risk management, their treasury management policies and practices should reflect this.

**Clauses formally adopted.**

1. This organisation will create and maintain, as the cornerstones for effective treasury management:

   - A Treasury Management Policy Statement, stating the policies, objectives, and approach to risk management of its treasury management activities.
   - Suitable Treasury Management Practices (TMPs), setting out the manner in which the organisation will seek to achieve those policies and objectives, and prescribing how it will manage and control those activities.
   - Investment Management Practices (IMPs) for investments which are not for treasury management purposes.

   The content of the policy statement TMPs and IMPs will follow the recommendations contained in Sections 6, 7 and 8 of the Code, subject only to amendment where necessary to reflect the particular circumstances of this organisation. Such amendments will not result in the organisation materially deviating from the Codes key principles.

2. This organisation (i.e., full Council) will receive reports on its treasury management policies, practices, and activities, including, as a minimum, an annual strategy and plan in advance of the year, a mid- year review and an annual report after its close, in the form prescribed in its TMPs and IMPs.

3. This council delegates responsibility for the implementation and regular monitoring of its treasury management policies and practices to Cabinet, and for the execution and administration of treasury decisions to the Chief Financial Officer, who will act in accordance with the organisations policy statement, TMPs, and IMPs and, if he/she is a CIPFA member, CIPFA’s Standard of Professional Practice on Treasury Management.

4. This Council nominates the Audit Committee to be responsible for ensuring effective scrutiny of the treasury management strategy and policies.

**APPENDIX 9 - Treasury Management Scheme of Delegation**

## (i) Full Council

1. Approval of the Treasury Management Strategy - prior to the new financial year
2. Approval of the Investment Strategy - prior to the new financial year
3. Approval of the MRP Policy - prior to the start of the new financial year
4. Approval of any amendments required to the Strategy during the year.
5. Receipt of a mid-year report on the Treasury Management Strategy, to include consideration of any recommendations of the Cabinet or Audit Committee arising from any concerns since the original approval.

## (ii) Cabinet

1. Developing and determining the Treasury Management Strategy, Investment Strategy and MRP policy and recommending them to full Council - prior to the start of the new financial year.
2. Receipt of a mid-year report on the Treasury Management Strategy and any concerns since the original approval and making recommendations to Council as appropriate.
3. Receiving, and reviewing reports on treasury management policies, practices, activities, and performance reports (based on quarterly reporting).
4. Approval of/amendments to the organisation’s adopted clauses, treasury management policy statement.
5. Budget consideration and approval.
6. Approval of the division of responsibilities.

### (iii) Audit Committee

1. Scrutinising the Council's Treasury Management Strategy, Investment Strategy and MRP policy, Treasury Management Policy Statement and Treasury Management Practices and making recommendations to Cabinet and Council as appropriate.
2. Receiving and reviewing monitoring reports (based on quarterly reporting) and making recommendations as appropriate.

**APPENDIX 10 - The Treasury Management Role of the Section 151 Officer**

Chief Finance Officer (S151 Officer) responsibilities:

- recommending clauses, treasury management policy for approval, determining Treasury Management Practices, reviewing the same regularly, and monitoring compliance
- submitting regular treasury management policy reports
- submitting budgets and budget variations
- receiving and reviewing management information reports
- reviewing the performance of the treasury management function
- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function
- ensuring the adequacy of internal audit, and liaising with external audit
- recommending the appointment of external service providers.

**Additional Responsibilities following new Codes of Practice/ Investment Guidance**

The above list of specific responsibilities of the S151 officer in the 2021 Treasury Management Code has not changed. However, implicit in the changes in both the Prudential and the Treasury Management Codes, is a major extension of the functions of this role, especially in respect of non-financial investments, (which CIPFA has defined as being part of treasury management). Namely:-

1. preparation of a capital strategy to include capital expenditure, capital financing, non-financial investments, and treasury management, with a long-term timeframe (say 20+ years – to be determined in accordance with local priorities).
2. ensuring that the capital strategy is sustainable, affordable, and prudent in the long term and provides value for money.
3. ensuring that due diligence has been carried out on all treasury and non-financial investments and is in accordance with the risk appetite of the authority.
4. ensure that the authority has appropriate legal powers to undertake expenditure on non-financial assets and their financing.
5. ensuring the proportionality of all investments so that the authority does not undertake a level of investing which exposes the authority to an excessive level of risk compared to its financial resources.
6. ensuring that an adequate governance process is in place for the approval, monitoring and ongoing risk management of all non-financial investments and long-term liabilities.
7. provision to members of a schedule of all non-treasury investments including material investments in subsidiaries, joint ventures, loans, and financial guarantees.
8. ensuring that members are adequately informed and understand the risk exposures taken on by an authority.
9. ensuring that the authority has adequate expertise, either in house or externally provided, to carry out the above.
10. creation of Treasury Management Practices which specifically deal with how non treasury investments will be carried out and managed, to include the following): -
    - Risk management (TMP1 and schedules), including investment and risk management criteria for any material non-treasury investment portfolios.
    - Performance measurement and management (TMP2 and schedules),

including methodology and criteria for assessing the performance and success of non-treasury investments.

- Decision making, governance and organisation (TMP5 and schedules), including a statement of the governance requirements for decision making in relation to non-treasury investments; and arrangements to ensure that appropriate professional due diligence is carried out to support decision making.
- Reporting and management information (TMP6 and schedules), including where and how often monitoring reports are taken.
- Training and qualifications (TMP10 and schedules), including how the relevant knowledge and skills in relation to non-treasury investments will be arranged.

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# Draft Capital Strategy (2024/25)

## Introduction

1. Hastings Borough Council has a range of capital resources at its disposal which is used in the delivery of its strategic priorities and objectives. These resources include iconic assets such as Hastings Castle and the Cliff Railways, to parks and open spaces, leisure facilities and entertainment venues.

2. The council's ability to ensure that these vital assets are well maintained is crucial to the future financial stability and resilience of the council. If assets fall into disrepair and are no longer fulfilling their maximum potential and primary purpose, then the ability to deliver our objectives and priorities is severely hindered.

3. The Capital Strategy should provide a high-level overview of how capital expenditure, capital financing, investments, liabilities and treasury management activity contribute to the provision of services. Together with an overview of how associated risk is managed and the implications for future financial sustainability.

4. It is therefore imperative that the council manages and plans its use of capital resources wisely and why one of the stated corporate objectives is to develop a full and detailed Corporate Asset Management Plan which will feed into future capital strategies, along with a Housing Strategy to deal with the Housing crisis that the Council finds itself in currently.

5. With all capital expenditure comes associated risk, and this comes in different forms and needs to be managed by the council when apprising different options. The risks could be from:

    - Will the Asset deliver the projected outcome?
    - Are the estimates for running costs and income accurate?
    - What is the most prudent way of financing the asset i.e. borrowing?

## Regulation

6. The CIPFA revised Prudential and Treasury Management Codes require all local authorities to prepare a capital strategy report, which seeks to provide the following:

    - a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services.
    - an overview of how the associated risk is managed.
    - the implications for future financial sustainability.

7. The aim of this capital strategy is to ensure that all elected members on the full Council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

8. This Capital Strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the Capital Strategy and the budget report. This ensures the separation of the core treasury function under security, liquidity and yield principles, and the policy and commercialism investments usually driven by expenditure on an asset.

9. The capital strategy seeks to identify:

   - The corporate governance arrangements for these types of activities:
   - Service objectives relating to the Capital expenditure:
   - The expected income, costs and resulting contribution:
   - The debt related to the activity and the associated interest costs:
   - The payback period (MRP policy):
   - For non-loan type investments, the cost against the current market value:
   - The risks associated with each activity.

10. Where a physical asset is being bought, details of market research, advisers used, ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

11. To demonstrate the proportionality between the treasury operations and the non-treasury operation, high-level comparators are identified.

12. The Capital strategy, and in particular the capital programme supports the Council's Corporate plan and is closely tied to the Medium-Term Financial Strategy and the budget. The Capital Strategy is required to be compiled for a longer timeframe – generally 10 to 20 years although not specified.

13. The Council's future spending plans are continuing to evolve and as such the Capital Strategy and other strategies may need to be re-determined by full Council when the future plans are sufficiently robust – given the impact of the Towns Fund monies and the potential housing schemes. The report does detail the Council's borrowing commitments until 2069/70 that result from past and current capital programmes.

## Objectives of the Capital Strategy

14. The Capital Strategy is one of the council's key documents in providing a medium to long term plan. It needs to be consistent with other key plans such as the following:

- Corporate Asset Strategy
- Corporate Plan
- Capital Programme
- Treasury Management Strategy

- Medium Term Financial Plan
- Revenue Budget
- Resources Plan

15. The Capital Strategy is therefore the policy framework document that sets out the principles to be used to guide the allocation of capital investment across all of the councils' priorities and informs the decisions on capital spending priorities.

16. In addition, and as part of the strategy, the Chief Financial Officer reports explicitly on the affordability and risk associated with the Capital Strategy.

## High Level Overview of how Capital Expenditure, Capital Financing and Treasury Management Activity Contribute to the Provision of Services

17. As detailed in the Council's Medium Term Financial Strategy (MTFS), the Council continues to be in a difficult financial position requiring service reforms in its journey to becoming a lower spending council. The Council seeks to use capital investment in the borough to not only achieve key corporate objectives but also to generate additional income in order to continue to provide services to its residents. The expenditure plans for the next three years are detailed below along with the expected outcomes.

### Capital Expenditure 2024/25

18. Capital Investment is defined as 'Expenditure on the acquisition, creation, or enhancement of 'non-current assets' i.e.items of land, property and plant which have a useful life of more than 1 year'. Expenditure outside of this definition will therefore be revenue expenditure.

19. The Council's Capital programme amounts to some £12.652m (£7.791m net of grants and contributions) in 2024/25. The major areas of expenditure include**:-**

    **(I) Housing Acquisition Programme (£11,866,000 of which £5.933m is expected to be spent in 2024/25)**
    A programme to potentially acquire up to 50 housing units of various bedroom sizes to use as Temporary Accommodation to reduce the cost to the council of using privately owned accommodation.

    **(II) Energy Generation – Unallocated (£4.3m of which £1.0m is expected to be spent in 2024/25)**
    An additional £4.3m has been allocated for energy generation projects but remains unallocated.

    **(III) Disabled Facility Grants (£2.056m (Est) – all grant funding)**
    Property related grants for adapting homes. In 2023/24
    the Council received funding of £2.1m. The figure for 2024/25 is not yet known – but is not expected to be less. Unspent grant from previous years can be carried forward to use for future spend.

**(IV) Annual programme of roof refurbishment (£1.7m of which £0.7m is expected to be spent in 2024/25)**
An annual programme of roof refurbishment is required for our commercial and industrial buildings to ensure they remain watertight for their tenants and the council is able to maintain their rental income over the coming years.

**(V) Energy – Solar Panels (£1.7m of which £0.5m is expected to be spent in 2024/25)**
The installation of solar panels on non-domestic rooftops within the borough – providing cheaper energy for businesses. An additional £4.3m has been allocated for energy generation projects in future years but remains unallocated.

**(VI) Priory Meadow Contribution to capital works (£250,000 for 2024/25)**
The Council owns 10% of the Priory Meadow shopping centre. The money represents its share of any capital investment costs for 2022/23. The Council receives 10% of the net income for the centre which provides a significant contribution towards meeting the service costs of the council.

**(VII) Pelham Crescent / Pelham Arcade – Building/Restoration Works (£1.1m in 2024/25)**
In line with the strategic priority of an attractive town, the council is working with property owners to restore the crescent and roadway. Much of the work is conditional on receipt of external grants and contributions.

**(VIII) IT Upgrade Programme (£600k of which £200k is expected to be spent in 2024/25)**
Working to upgrade the IT Systems – Anticipating spend of £100k on Hardware and £100k on Software in 2024/25.

**(IX) Groyne Refurbishment (£35k for 2024/25)**
Preserving sea defences and the town is a key priority. The Council funds the groyne refurbishment/ sea defence works and sets aside £35,000 p.a. for this – sometimes packaged together over several years.

## Capital Expenditure 2025/26

20. The 2025/26 Capital programme amounts to some £6.090m (£3.4m net of grants and contributions).

21. The main areas of expenditure are Disabled Facility Grants (£2.056m fully grant funded), Energy Generation (£1.8m unallocated, £638k for Solar Panels), Annual programme of roof refurbishment (£500k), Pelham Arcade (£600k), Priory Meadow (£250k), IT Upgrade Programme (£200k) and Groyne refurbishment (£35k).

## Capital Expenditure 2026/27

22. The Council's current capital expenditure plans for 2026/27 amount to some £3.8m (£1.7 net of grants and contributions).

23. The main areas of expenditure are currently Disabled Facility Grants (£2.056m fully grant funded), Energy Generation Unallocated (£1m), IT Upgrade Programme (£200k), Annual programme of roof refurbishment (£500k) and Groyne Refurbishment (£35k).

## Summarised Capital Expenditure and Funding - 2023/24 to 2026/27

24. The table below shows a summary of the expenditure for the current and next three years, along with the projected borrowing requirements.

| | 2023/24 Forecast £'000 | 2024/25 Estimate £'000 | 2025/26 Estimate £'000 | 2026/27 Estimate £'000 |
|---|---|---|---|---|
| **Gross Capital Expenditure** | 17,144 | 12,652 | 6,090 | 3,799 |
| **Funded By** | | | | |
| Capital Grants & Contributions | 8,907 | 4,861 | 2,433 | 2,064 |
| S106 | 271 | 0 | 0 | 0 |
| Capital Receipts | 2,579 | 5,130 | 300 | 50 |
| Other Funding | 5,387 | 2,661 | 3,357 | 1,685 |
| **Total** | **17,144** | **12,652** | **6,090** | **3,799** |

**Financing the Capital Programme**

25. The Council can invest in a capital programme so long as its capital spending plans are "affordable, prudent and sustainable".

26. The main sources of finance for capital projects are as follows:

- Capital receipts (from asset sales)
- Capital grants (e.g. Disabled Facilities Grant)
- External contributions (e.g. Section 106 developers' contributions)
- Earmarked Reserves
- Revenue contributions
- Borrowing including internal (Capital Financing Requirement).

27. Borrowing (or Capital Financing Requirement) makes up the most significant element. While the Council has sufficient cash and investment balances in the near term it is able to internally borrow but, in the future, will need to borrow externally in addition to the estimated £64.9m borrowing which will be outstanding at 31 March 2024.

28. The Capital Financing Requirement is reduced over the life of individual assets by an annual contribution from revenue (Minimum Revenue Provision). Further information including borrowing forecasts, the provision for the repayment of debt, and borrowing limits are set out in the Treasury Management Strategy. The table below shows the projected indebtedness of the Council based on the current Capital programme and expected levels of capital receipts, grants and contributions.

**Table: Capital Financing Requirement (CFR) less Minimum Revenue Provision (MRP)**

| CFR | 2022/23 (Unaudited) £'000s | 2023/24 (Estimate) £'000s | 2024/25 (Estimate) £'000s | 2025/26 (Estimate) £'000s | 2026/27 (Estimate) £'000s |
|---|---|---|---|---|---|
| CFR-Opening | 71,970 | 71,099 | 70,195 | 69,229 | 68,208 |
| Less MRP | (870) | (904) | (966) | (1,021) | (1,125) |
| Plus, New Borrowing | - | - | - | - | - |
| **CFR Closing** | **71,099** | **70,195** | **69,229** | **68,208** | **67,083** |

29. The table above highlights that by the end of 2025/26 the level of debt will have reduced to some £68.2m (subject to viability and the approval of schemes within the Capital programme).

**Revenue Consequences of the Capital Programme on the General Fund**

30. Borrowing has long term revenue consequences. The overall indebtedness of the Council is reduced by the MRP each year. The overall level of debt needs to be viewed against the overall Long-Term Assets of the authority which stood at £191.9m at 31 March 2023 (unaudited) (£185.4m as at 31 March 2022).

31. The Council have significantly reduced the borrowing requirement over the last 2 years will need to continue to carefully consider the structure and timing of any new borrowing to ensure debt does not exceed the CFR in the years ahead.

**Financial Risk Management**

32. The treasury management strategy outlines in some detail the economic environment and the risks that the Council faces in managing its investments and borrowing activities.

33. Where borrowing money to finance economic development or regeneration schemes the Council is increasingly dependent upon the income streams to finance the debt repayments. No matter how good the business cases, and how much of the debt is at fixed rates, there is a limit to the exposure that is acceptable without putting the Council at complete risk of being unable to provide key services in the event of a significant recession.

34. To arrive at an overall borrowing level (Authorised and Operational borrowing limits), the Council needs to take a considered view of its other potential liabilities, future borrowing requirements, guarantees and loans given, bad debts, claims against the Council, future funding, security and diversity of the existing income streams, and unforeseen events e.g. a pandemic.

35. The full Council determine the total limits on borrowing.

36. In terms of cash backed investments, the Investment Policy provides strict guidance on the counterparties the Council is prepared to invest with and for what periods. The Council invested £2m in a property fund (CCLA) in April 2017 and a further £3m tranche of monies in a diversified investment fund in 2020/21.

37. In terms of asset backed investments and projects e.g. involving commercial property and housing, the business cases look to identify the alternative options and uses of the premises should they become vacant.

38. Some projects such as the solar panel installations have some asset backed values, but the ability to meet the debt repayments from energy savings and sale of the surplus energy will remain a risk unless long term forward sale agreements are made. However, such long-term agreements come at the cost of not necessarily obtaining the maximum income. A balance of risk and reward needs to be achieved.

**Loans and Guarantees**

39. The Council is required to maintain a schedule of loans and guarantees to other organisations.

**Table: Loans to Other Organisations**

| 3rd Party Organisations | Rate/ Return (%) | Start Date | End Date | Principal Outstanding as at 31/03/2024 £ | Type |
|---|---|---|---|---|---|
| Amicus /Optivo | 3.78% | 04/09/2014 | 02/09/2044 | £1,788,235 | Maturity |
| The Foreshore Trust (504807) | 1.66% | 21/03/2016 | 20/03/2026 | £79,712 | Annuity |
| The Source | 2.43% | 17/12/2015 | 17/12/2025 | £8,144 | Annuity |
| | | | **Sub-Total** | **£1,876,091** | |
| **Hastings Housing Company** | | | | | |
| Hastings Housing Company - Loan 1 | 4.48% | 28/02/2018 | 28/02/2058 | £784,676 | Maturity |
| Hastings Housing Company - Loan 2 | 4.84% | 12/02/2019 | 12/02/2059 | £344,810 | Maturity |
| Hastings Housing Company - Loan 3 | 4.84% | 13/06/2019 | 13/06/2059 | £4,359,912 | Maturity |
| | | | **Sub-Total** | **£5,489,398** | |
| | | | **Total** | **£7,365,489** | |

40. The above table shows a series of loans to the Hastings Housing Company in respect of property purchases. As at 31 December 2023 the Capital loans amount to £5,489,398. The company has access to a revenue loan facility from the Council; the company fully repaid the revenue loan but has outstanding commitments regarding the capital advances.

41. The Housing Service provides loans and guarantees to individuals for rent in advance and rental deposits and the Council also provides a limited loan facility to staff for car loans, season tickets, and bicycle loans.

42. The Council has other liabilities that need to be considered when assessing the overall financial position of the Council e.g. potential legal claims, pension liabilities.

**Reserves**

43. The Council maintains reserves for specific purposes (earmarked reserves) and also a general reserve for unavoidable future liabilities. The minimum recommended level of reserves to be maintained has been set at £4m. The adequacy of the reserve levels are reviewed on a regular basis, and particularly when determining the budget.

## Risk Appetite & Prudential Indicators

### Internal Borrowing

44. When undertaking Capital projects or purchasing new assets, the Council has a number of options as to when and how to finance these. If there are no grants or revenue resources and no capital receipts the Council will finance by borrowing. If it delays the borrowing, then it will be using its own monies (Internal borrowing - generally from reserves) to temporarily fund the assets.

45. If an authority has a large internal borrowing position, this will mean that reserves and balances have temporarily been used to support borrowing positions and therefore the reserves will not be backed by cash in the bank. This position continues to work for many, but as reserves and balances are utilised in the years ahead and balances fall, this will reduce any ability to internally borrow and may bring forward the need to borrow externally (potentially at a time of high interest rates, or when there is limited ability to borrow externally).

46. The Council's Treasury advisers undertook a review of client's balance sheets and the average level of internal borrowing was, from the above graph, just under 20%. The level will vary depending upon when an authority finances expenditure

and when debt is refinanced.

47. For Hastings Borough Council it has historically sought to achieve near full financing of the Capital programme over previous years in order to take advantage of the historically low borrowing rates and avoid the risk of having to lock into high interest rates when it has no option but to borrow.

48. For the last few years, a higher level of internal borrowing was adopted. Currently, with interest rates having risen considerably from historic lows, and looking likely to stay at that level for the next financial year the Council will need to carefully consider when the best time to borrow is. Guidance from our external treasury managers will be sought before any borrowing decision are made.

49. For 2024/25 the level of internal borrowing by year end is expected to be £2.7m out of a total borrowing requirement of some £69.2m (3.8%).

## Gearing

50. Gearing has predominantly been a debt metric used by the private sector more than the public sector, but recent moves towards commercialism opportunities and investments means that borrowing is a much greater risk and gearing is an appropriate prudential indicator.
Gearing provides an early indication of where debt levels are rising, relative to long-term assets held.

**Table showing Future Projections of Gearing Ratios – based on Capital programme**

| Gearing Calculation | Actual 2021-22 £'000 | Actual 2022-23 £'000 | Estimate 2023-24 £'000 | Estimate 2024-25 £'000 | Estimate 2025-26 £'000 | Estimate 2026-27 £'000 | Operational Boundary £'000 |
|---|---|---|---|---|---|---|---|
| Capital Expenditure | | | 17,144 | 12,652 | 6,090 | 3,799 | |
| Additional Financing Required | | | 5,387 | 2,661 | 3,357 | 1,685 | |
| Net Assets | 108,409 | 149,497 | 166,641 | 179,293 | 185,383 | 189,182 | 179,293 |
| Long Term Assets | 185,420 | 191,939 | 209,083 | 221,735 | 227,825 | 231,624 | 305,084 |
| Capital Financing Requirement | 71,790 | 71,099 | 70,195 | 69,229 | 68,208 | 67,083 | 135,000 |
| **Ratios:** | | | | | | | |
| **Debt : Net Assets** | **66%** | **48%** | **42%** | **39%** | **37%** | **35%** | **75%** |
| **Debt : Long Term Assets** | **39%** | **37%** | **34%** | **31%** | **30%** | **29%** | **44%** |

Note: Outturn figures for 2021/22 and 2022/23 are unaudited

51. The Council's position will move from 37% to 29%. If the Council borrowed at the limits to its current Operational Boundary (£135m), then debt to long term assets ratio could rise to 44%.

52. All decisions around debt comes back to affordability, prudence and sustainability principles which are at the heart of the Prudential Code and have been since its inception in 2004.

53. The Chartered Institute of Public Finance and Accountancy have issued a clear statement on the levels of debt that Councils in general are accumulating following the purchase of commercial assets in particular. Such borrowing must be proportionate to the size of the authority. Further detailed guidance was released in autumn 2019, and further changes to the Treasury Management codes have been undertaken to produce revised 2021 editions.

54. The government revised their lending criteria for the Public Works Loan Board (PWLB) on the 25 November 2020 which effectively prevents Councils from borrowing for commercial property investments where the primary purpose is to make a return (yield). The Council has no intention of purchasing commercial property primarily for yield and were it to consider doing so it would need to seek full Council approval to do so.

**Ratio of Financing Costs to Net Revenue Stream**

55. Financing costs are the element of the budget which an authority is committed to, even before they have run a single service or incurred any other costs as they reflect the current costs of previous/planned capital financing decisions.

56. In Hasting's case the ratio of financing costs in 2024/25 represents, 11%, of the Net Revenue Stream which leaves 89% of the revenue stream for all the other services to be provided. The higher the percentage, therefore, the less is left for running services.

57. If the Net Revenue Stream is reducing, as funding sources are reduced over time, then even though financing costs may be fixed through fixed-term loans and interest rate certainty, the ratio will potentially continue to climb leaving less available for front-line services and placing further pressures on budget positions.

58. However, the income the Council receives from rents and fees and charges decreases the net expenditure of the Council. The calculation of debt charges to "the amount to be met from Grant and Collection Fund" as a proxy for the "Net Revenue Stream" therefore has to be treated with considerable caution.

59. This leads back then to local decision making and the need/objectives behind capital investment. Business cases must identify ongoing revenue implications and hence affordability. The Treasury Management Strategy includes a prudential indicator that identifies the ratio of financing costs to Net Revenue Stream. This is a further way of ensuring that affordability, prudence and sustainability considerations are kept to the fore in treasury reporting.

## Corporate Governance Arrangements – Project Approval Process

60. The Council has to update its current Corporate Plan, but it remains important that the capital programme remains realistic in terms of resources and timescales to achieve the desired outcomes.

61. The Council has a number of project management procedures and tools in place for managing individual projects. Key is the project initiation stage, the approval process and thereafter effective performance monitoring and reporting. A business case is required and a detailed report to Cabinet/Council. Any new Capital proposal requires full Council approval.

62. Major projects are likely to have impacts on other key services such as Legal, Finance and Estates teams depending upon the nature of the projects. External support is commissioned where there is insufficient capacity, knowledge, or expertise within the Council. Cabinet and the Overview and Scrutiny Committee receive quarterly updates on financial performance (including the capital programme).

63. Property developments and purchases are considered by Cabinet, and are subject to full Council approval, with delegated authority normally provided thereafter to the Chief Finance Officer in consultation with the leader to negotiate the final terms. The Council's legal team, surveyors and Corporate Property Officer are all closely involved. The Council will normally employ the services of an agent to advise on the price and conduct negotiations. Necessary due diligence is conducted and external specialist surveyors and advisors employed as necessary.

## Knowledge, Skills and Training

64. In order to deliver the Capital Programme, it is essential that the Council has access to the right knowledge and skills. The Council employs fully qualified and experienced staff such as solicitors, estate managers, surveyors and accountants.

65. The Council maintains a training budget, recognising that it remains critical to the organisation to have a well-trained and motivated workforce. The Council provides on-line training courses, internal and external training, to enable staff to complete their Continuing Professional Development (CPD) requirements.

66. The Council seeks to ensure members have access to training opportunities in order for them to adequately undertake their governance role. Workshops and training events are held on a regular basis.

67. Where specialist knowledge is required, the Council will obtain expert advice, particularly around property specialisms, taxation, and legal advice.

## Chief Finance Officer Report

68. Within the Prudential Code it is the responsibility of the Chief Finance Officer to explicitly report on the delivery, affordability and associated risks to the strategy.

## Delivery

69. The delivery of the individual schemes in the Capital Programme are directly linked to the original approval and business case for each individual project which has an assigned project manager responsible for delivery.

70. As part of the quarterly financial update report the performance of individual projects are presented to Overview and Scrutiny along with all other financial performance.

## Affordability

71. Affordability is critical in applying the capital strategy and approving projects for inclusion in the capital plan. This is mostly demonstrated by a specific report on the project being presented to council for approval supported by a business case identifying the expenditure and funding, appraisal of alternative options and the risks and rewards for the approval of the scheme.

72. The Capital programme is not heavily reliant on borrowing currently and will continue to be focused on its financial stability longer term and will always seek to secure external funding wherever possible to help reduce borrowing costs.

73. Where borrowing is to be used, the affordability is key, and that affordability has to include the interest costs of that borrowing and the provision for the repayment of the borrowing. This repayment is matched to a prudent asset life and any income streams estimated to fund this asset must be sustainable. The "rules" around the governance of this borrowing is outlined in the prudential code.

74. At no stage should the asset value be lower than the value of outstanding debt, other than for a short period, unless there is a clear plan to mitigate that shortfall or to sell that asset.

75. The Council's existing borrowing levels are not considered excessive. However, a downturn in the economy with resultant loss of income would require the Council to make greater service cuts to balance the budget.

## Risks

76. The risks associated with individual projects are identified and mitigated as part of the initial business case development stage and reported through both the financial reporting process to Overview and Scrutiny as well as being included as part of the Corporate risk register.

77. There are clear links from the capital plan to both the treasury management strategy, prudential indicators, authorised borrowing limits and the revenue budget. These are also subject to review and oversight by members at Audit Committee and Council.

78. For any new borrowing, and this is a greater risk as the value of borrowing increases, this increases the councils overall liabilities that will need to be repaid in the future. In addition, this increases the Council's level of fixed interest and repayment costs that it will incur each year. This is a clear risk that all members need to be aware of.

79. However, this risk for all assets is mitigated by a robust business case and a full MRP that will repay the borrowing costs over a (prudent) asset life. Any variation in expected income is an issue, however given the wide range of operational assets and different income streams this is not considered a significant risk.

80. This Capital Strategy and the Treasury Management Strategy is likely to be reviewed and updated during the year, and put before full Council, as and when the Council's spending plans are developed further.

## Conclusion

81. The current system of borrowing is still a self-regulatory system which means that responsibility for borrowing decisions, and the level of borrowing incurred by a Council are determined at a local level.

***"..the responsibility for decision making and ongoing monitoring in respect of capital expenditure, investment and borrowing, including prudential indicators, remains with full Council". (Prudential Code December 2017).***

82. The Chief Finance Officers' personal view is that borrowing decisions result in a long-term commitment to fund that borrowing, and that all decisions are made as a whole programme perspective and not on an individual basis.

83. However, for transparency and ease of comparison between projects, indicative full figures for borrowing will always be included in all business cases brought forward for decision making regardless of whether or not borrowing will actually be required.

## Consultation and Communication

84. The detailed Capital Programme is included within the Council's budget which was agreed on 21st February 2024. The programme supports the Council's current Corporate Plan, which is due to be updated in due course, at which time the Capital programme may well be amended to align with the overall Corporate Strategy and in line with the new Asset Management Plan.

85. The budget for 2024/25 was subject to public consultation.

## Equality Impact Assessment

86. Equality Impact assessments are considered as part of the business case when considering individual capital proposals.

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