

**Agenda Item No:**

**Report to:** Cabinet

**Date of Meeting:** 11 February 2019

**Report Title:** Treasury Management, Annual Investment Strategy and Capital Strategy 2019/20

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**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 Cabinet and 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 has some £46.7 million of debt (as at 1 January 2019), and investments which can fluctuate between £15m and £30m in the year. The level of debt is set to increase to some £78m by 2020/21.

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**Recommendations**

**Cabinet recommends to full Council that:**

- 1. The Council approve the Treasury Management Strategy, Minimum Revenue Provision (MRP) Policy, Annual Investment Strategy, and the Capital Strategy.**
- 2. That the strategies be updated as necessary in 2019/20 in the light changing and emerging risks, the Council's evolving future expenditure plans, along with further expected guidance on the Codes of Practice and government regulations.**
- 3. That the Financial rules and the Financial Operating Procedures of the Council are reviewed and revised (as necessary) to meet the new requirements of the Code.**
- 4. That the Investment Policy includes the use of CCLA's Diversified Income Fund with a limit of up to £3m being invested within it (£5m in total with CCLA).**

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## Reasons for Recommendations

The Council seeks to minimise the costs of borrowing and maximise investment income whilst ensuring the security of its investments. The Council continues to make substantial investments in commercial property, housing and energy generation initiatives, and this will continue to involve the Council in taking on additional borrowing.

The sums involved are significant and the assumptions made play an important part in determining the annual budget. The CIPFA Code of Practice (2017 Edition), adopted by the Council last year, was released to take account of the more commercialised approach being adopted by councils and the enhanced levels of transparency required. The Code represents best practice and helps ensure compliance with statutory requirements.

The Council has the ability to diversify its investments and must consider carefully the level of risk against reward against a background still of historically low interest rates. 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.

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## Introduction

1. 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.
2. 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.
3. 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"
4. In December 2017, CIPFA issued a revised Treasury Management Code of Practice and a revised Prudential Code. These revisions have particularly focused on non-treasury investments and especially on the purchase of property with a view to generating income. Such purchases could involve undertaking external borrowing to raise the cash to finance these purchases, or the use of existing cash

balances. Both actions would affect treasury management. As the Localism Act 2011 only gave English local authorities a General Power of Competence, these changes in the revised codes are particularly relevant therefore to the activities of English authorities.

5. CIPFA issued a statement that accepted that the issue of revised codes in the late stages of setting the 2018-19 budget cycle was not helpful and accordingly, full implementation was not expected until 2019-20 across all authorities.
6. The Chief Finance Officer responsibilities have been extended to include a series of new roles in respect of the capital strategy and also a specific role in respect of investment in non-financial assets. Amendments are included within the Appendices.
7. Treasury Management Practices and Financial Operating Procedures will need to be reviewed to ensure they properly take account of changes required by the Codes and government regulations.
8. The Audit Committee considered the same report and strategies at its meeting on the 23 January and resolved to recommend the policies and strategies to Cabinet and full Council.

## **Investment guidance**

9. In early 2018 the Ministry of Housing, Communities and Local Government (MHCLG) issued new statutory guidance on local government investments). This provided for added focus on non-financial asset investments and includes for example loans made to wholly-owned companies, third parties, joint ventures.
10. Investments made by a local authority can be classified into one of two main categories:

### **(i) Investments held for treasury management purposes**

Where treasury management investments are held the Council discloses the contribution these investments make to the local authority

### **(ii) Other investments**

Councils are required to disclose the contribution that all other investments make towards the service delivery objectives and /or place making role of the authority. Each authority is able to define the types of contribution that investments can make and a single investment can, make more than one type of contribution. These include:

- Yield/profit
- Regeneration
- Economic benefit/business rates growth
- Responding to market failure
- Treasury management

## Minimum Revenue Provision (MRP) guidance

11. The MHCLG issued new MRP guidance in early 2018. This provided new focus on expenditure relating to purchasing non-financial asset investments and limiting the periods over which assets could be financed. This materially affected the Council's Housing Company and particularly any monies that constitute equity (limited to 20 years). It does not affect the Council's ability to lend monies to the Housing company over a 40 year loan period – unless the assets have an estimated useful life of less than that.

## The Primary Requirements of the Code

12. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
13. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
14. 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.
15. 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.
16. 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.
17. Publication of the Strategies on the Council's website.

## Reporting Arrangements

18. The reporting arrangements proposed, in accordance with the requirements of the 2017 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,

19. The latest CIPFA Code of Practice on Treasury Management (2017) was adopted by this Council in February 2018. The main clauses adopted are included in Appendix 8.
20. 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.

## Investment Performance 2018-19

21. The performance for the first 9 months of 2018/19 provided an average return of 0.65%. This compares to 0.34% for the same period last year. These figures exclude the interest receivable in respect of loans to other organisations.
22. The total interest receivable for the first 9 months is £117,000 (2017/18 £67,000). These figures exclude the interest receivable in respect of the three loans to other organisations and income from the Property Fund investment. If all the interest received is included this would amount to some £253,000 (2017/18 £178,500).
23. The Cabinet on 7 January 2019 considered a Mid-Year report on Treasury Management based on the performance and activities arising since setting the strategies before the start of the financial year. The current strategy and policies were considered to be appropriate and no changes were made.

## Capital Strategy

24. In the light of the increasing commercialisation within local government in particular, in December 2017, CIPFA issued revised Prudential and Treasury Management Codes.

25. The codes require all local authorities to produce detailed Capital Strategies.
26. 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.
27. 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.
28. 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.
29. 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
  - 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.
30. 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.
31. The Capital Strategy would look to cover a much longer planning period than the existing capital programme. Work has commenced on identifying likely future expenditure and as the Council's plans evolve the capital strategy and all the prudential indicators and controls e.g. borrowing limits will need to be determined by full Council.

## **Risk Management**

32. 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 last six years as and when these have been further developed by its advisers.

33. 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.
34. 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. Further training sessions for all members will be arranged prior to the consideration of the future Mid-year review by the Audit Committee and Cabinet.
35. The training needs of treasury management officers will also be reviewed in the light of the Code's requirements and experience of new staff.
36. The additional risks that the Council is taking 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. Pier claim, rates revaluation, robustness of income streams, loans and guarantees to other parties, 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.
37. 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 Asset Services) ratings advice.
38. The security of the principal sum remains of paramount importance to the Council.

## **Economic/Financial Implications**

39. The Council generally has investments in the year of between £15 million and £30 million at any one time, and is estimated to have longer term borrowings approaching £60m by the end of March 2019. 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**

40. 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 new Capital Strategy.

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

Action	Key milestones	Due dates (provisional)	Responsible
Update Treasury Management Practices, produce necessary schedules for full compliance with Codes of Practice	1 April 2019	Full implementation by 2019/20	Chief Finance Officer
Arrange Training for members/ officers	Year End & Mid-Year Review Report	July 2019	Chief Finance Officer

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#### Wards Affected

None

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#### Area(s) Affected

None

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## Policy 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	Yes
Local People's Views	No

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### Documents Attached:

(i) Treasury Management Strategy (including Investment Policy)

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) Capital Strategy

### Other Supporting Documents:-

CIPFA - Treasury Management Code of Practice (2017)

CIPFA - The Prudential Code (2017)

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