

Report To: Cabinet

Date of Meeting: 7 February 2022

Report Title: Treasury Management, Annual Investment Strategy and Capital Strategy 2022/23

Report By: Peter Grace
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 some £66.06 million of external debt (as at 31 March 2022), and investments which can fluctuate between £15m and £30m in the year. The level of debt is set to increase to some £90m by 2023/24.

Recommendations

Cabinet recommend to Budget Council that:

- A. The Council approve the Treasury Management Strategy, Minimum Revenue Provision (MRP) Policy, Annual investment Strategy and the Capital Strategy.**
- B. The strategies listed are updated as necessary during 2022/23 in the light changing and emerging risks and the Council's evolving future expenditure plans.**
- C. The Financial Rules and the Financial Operating Procedures of the Council are reviewed and revised as necessary to meet the requirements of the Code of Practice.**

Reasons for Recommendations

1. 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 property, housing and energy generation initiatives, and this will continue to involve the Council in taking on additional borrowing.
2. The sums involved are significant and the assumptions made play an important part in determining the annual budget. The CIPFA Treasury Management Code of Practice (2017 Edition), previously adopted by the Council, was released to take 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.
3. The Council has the ability to diversify its investments and must consider carefully the level of risk against reward against a background of historically very 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. 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

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. 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 balance.
4. 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"

5. The Chief Finance Officer responsibilities were recently 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. The details are included within the Appendices.
6. The Audit Committee considered a similar report and the strategies at its meeting on the 13 January 2022 and after careful consideration resolved to recommend the policies and strategies to Cabinet and Council.

Changes to the CIPFA 2017 Prudential and Treasury Management Codes

7. CIPFA has again been looking at revising the Prudential Code and Treasury Management Code and undertaken a number of consultations. These follow "ongoing concerns over local authority commercial investments", CIPFA said.
8. The Prudential Code is used to ensure that capital finance decisions are sustainable, while the Treasury Management Code sits alongside to provide a framework for risk management.
9. Following the conclusion of the consultations CIPFA published revised codes on 20th December 2021 and has stated that formal adoption is not required until the 2023/24 financial year. This Council 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.
10. The revised codes will have the following implications:
 - A requirement for the Council to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement;
 - Clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment;
 - Address ESG issues within the Capital Strategy;
 - Require implementation of a policy to review commercial property, with a view to divest where appropriate;
 - Create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices);
 - Ensure that any long term treasury investment is supported by a business model;

- A requirement to effectively manage liquidity and longer term cash flow requirements;
- Amendment to TMP1 to address ESG policy within the treasury management risk framework;
- Amendment to the knowledge and skills register for individuals involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each council;
- A new requirement to clarify reporting requirements for service and commercial investment, (especially where supported by borrowing/leverage).

11. In addition, all investments and investment income must 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 a council'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.

12. As the Treasury Management Strategy Statement and Annual Investment Strategy deals solely with treasury management investments, the categories of service delivery and commercial investments will be dealt with as part of the Capital Strategy for 2023/24.
13. The revisions will strengthen both codes with a greater focus on climate and environmental, social and governance risks when making financial decisions. There is also guidance on CIPFA's stance that borrowing for investment return, or debt for yield, is an imprudent activity that puts public money at undue risk.
14. The key changes clarify and update CIPFA's position on local authority commercial investment. The revised code emphasise that any borrowing made solely for the

purpose of financial return constitutes imprudent activity, while also taking into account the realities that accompany regeneration activities.

15. To ensure local authorities can implement the code changes in a smooth and orderly fashion CIPFA is proposing a soft implementation in 2022/23. CIPFA will expect full implementation by 2023/24. Further details of the changes to the Prudential Code and Treasury Management Code are discussed in the Treasury Management Strategy.
16. The CIPFA Code of Practice on Treasury Management (2017) was adopted by this Council in February 2018. The Council will be asked to adopt the revised 2021 addition of the Code, with the aim of achieving full compliance, for 2023/24.

Borrowing / Borrowing Levels

Investment guidance

17. 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.
18. 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

The Primary Requirements of the Code

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

20. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.
21. 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.
22. 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.
23. 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.
24. Publication of the Strategies on the Council's website.

Reporting Arrangements

25. 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,

26. The 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.
27. 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

28. In the light of the increasing commercialisation within local government in particular, in December 2017, CIPFA issued revised Prudential and Treasury Management Codes.
29. The codes require all local authorities to produce detailed Capital Strategies.
30. 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.
31. 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.
32. 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.
33. 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
34. 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.
35. 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.

36. 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.

Risk Management

37. 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.
38. 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.
39. 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.
40. The training needs of treasury management officers will also be reviewed in the light of the Code's requirements and experience of new staff.
41. 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.
42. 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.
43. The security of the principal sum remains of paramount importance to the Council.

Economic/Financial Implications

44. 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 £66.1m by the end of March 2022 (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

45. 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.
46. 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.
47. 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.
48. 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 Year Mid-Year Review and prior to setting strategies for the forthcoming year Report	July 2022 & January 2023	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 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 (2021)
CIPFA - The Prudential Code (2021)
Budget Report - Cabinet 7 February 2022

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