

<p style="text-align: center;"><b>AUDIT COMMITTEE (30<sup>th</sup> January 2019)</b></p> <p style="text-align: center;"><b>&amp;</b></p> <p style="text-align: center;"><b>FULL COUNCIL (26<sup>th</sup> February 2019)</b></p>	
<p><b>Report of:</b> Neville Murton, Corporate Director Resources</p>	<p><b>Classification:</b> Unrestricted</p>
<p><b>Capital Strategy Report, Treasury Management Strategy Statement and Investment Strategy Report for 2020/21</b></p>	

### **REASONS FOR URGENCY**

There has been a significant delay in producing the 2018/19 accounts due to the complexities of resolving the issues identified by Deloitte that were reported to the July Audit Committee. This has led to a requirement to seek external validation of some key figures contained in the Treasury Management Strategy Statement and the Capital Strategy Report, such as the Minimum Revenue Provision. This, added to difficulties in staffing, has led to the report not being produced and published five clear working days of the meeting. The Policies need to be approved by this Audit Committee, before going to Council on the 20<sup>th</sup> February 2020, as the Policies need to be approved before the start of 2020/21 financial year.

#### **Executive summary**

- 1) This report fulfils the Council's legal obligation under the Local Government Act 2003 to have regard to both the CIPFA Code and the MHCLG Guidance on Treasury Management.
  
- 2) The Council is required by legislation and guidance to produce three strategy statements in relation to its treasury management arrangements. The three statements are:
  - a) a Treasury Management Strategy Statement which sets out the Council's strategy for the management of the Council's treasury investments and debt portfolio, including potential new borrowing, for the financial year and establishes the parameters (prudential and treasury indicators) within which officers under delegated authority may undertake such activities;
  - b) an Investment Strategy which sets out the Council's service and commercial investments, its policies for managing existing investments and the governance/decision-making arrangements for new investments; and,
  - c) a Capital Strategy Report which sets out an overview of how the Council's capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability.

- 3) This report also covers the requirements of the 2017 Prudential Code, including setting of Prudential Indicators for 2020/21, which ensure that the Council's capital investment decisions remain affordable, sustainable and prudent. The Prudential Code also requires the production and approval of an annual Capital Strategy.
- 4) The Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA TM Code) which requires the Authority to approve a treasury management strategy statement before the start of each financial year.
- 5) The Ministry of Housing, Communities and Local Government (MHCLG) issued revised Guidance on Local Authority Investments in February 2018 that requires the Authority to approve an investment strategy before the start of each financial year.
- 6) Clear delegated responsibility for overseeing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions is required. For this Council the delegated body is the Audit Committee. Officers will report details of the Council's treasury management activity to the Audit Committee at each of its meetings during the year. Additionally, a mid-year and full-year report will be presented to Full Council.
- 7) 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. Training will be arranged as required for members of the Audit Committee who are charged with reviewing and monitoring the Council's treasury management policies. The training of treasury management officers is also periodically reviewed and enhanced as appropriate.

## **Recommendations**

It is recommended to Council to:

- 1) Approve and adopt the following policy and strategies:
  - a) The Treasury Management Strategy Statement contained in Appendix A;
  - b) The Investment Strategy contained in Appendix B;
  - c) The Capital Strategy Report contained in Appendix C;
  - d) the Prudential and Treasury Management indicators contained in Appendix D; and,
  - e) the Treasury Management Policy Statement as set out in Appendix E.
- 2) Note that the Approved Limit for loans to local charities for service purposes of £0.6m was exceeded by £0.4m in 2019/20, as the approved limit did not consider a pre-existing loan to one charity, as set out in section 3.5 of the Investment Strategy, Appendix B. This limit has been suitably adjusted

## **1 REASONS FOR THE DECISIONS**

- 1.1 The Council has adopted the relevant CIPFA Treasury Management and Prudential Codes, and follows the MHCLG Investment Guidance, as required to comply with the Local Government Act 2003. The guidance prescribes the production of three strategy documents, to be approved by the Council before the start of the financial year to which they relate.
- 1.2 The Prudential Code for Capital Finance in Local Authorities (2017) produced by CIPFA guides the Council in the production of a framework designed to ensure that the Council's capital expenditure and financing plans are prudent, sustainable and affordable
- 1.3 The Treasury Management in the Public Services: Code of Practice (2017) produced by CIPFA guides the Council in setting a risk management framework for the management of its surplus cash and new and existing borrowing.
- 1.4 The MHCLG Investment Guidance guides the Council in setting a decision-making, governance and risk management policy for its service and commercial investments.
- 1.5 The three strategy documents that the Council should produce are:
  - Treasury Management Strategy, including prudential indicators
  - Investment Strategy
  - Capital Strategy.

## **2 ALTERNATIVE OPTIONS**

- 2.1 The Council is bound by legislation to have regard to the CIPFA Codes and MHCLG Investment Guidance. If the Council were to deviate from those requirements, there would need to be some good reason for doing so. It is not considered that there is any such reason, having regard to the need to ensure that the Council's capital investment plans are affordable, sustainable and prudent, and its treasury management activity is managed within an adequate risk control framework.

## **3 DETAILS OF THE REPORT**

### **3.1 Background to Treasury Management**

- 3.2 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 primarily before considering investment return. A portion of the investment balance is invested on a long term basis to preserve purchasing power and generate higher returns to support the revenue budget.

- 3.3 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 the Council 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.

- 3.4 CIPFA defines treasury management as:

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

- 3.5 The Treasury Management Strategy Statement report forms part of an annual cycle of Committee and Council reports. The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of policies, estimates and actuals.

3.5.1 **A treasury management strategy statement** (Appendix A)

3.5.2 **A mid year treasury management report** – This will update members with the progress of the capital position, amending prudential indicators as necessary, and whether any policies require revision.

3.5.3 **A treasury outturn report** – This provides details of annual actual prudential and treasury indicators and annual actual treasury operations compared to the annual estimates within the strategy.

3.6 The Council uses Arlingclose Limited as its external treasury management. The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and officers will ensure that undue reliance is not placed upon the external service providers.

3.7 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. Training will be arranged as required. The training needs of treasury management officers are periodically reviewed.

### 3.8 **The 2019/20 Strategy and Current Investment Position and Performance**

3.9 The Strategy for 2019/20 was approved by Full Council in February 2019 and the Audit Committee received a Treasury Management mid year review on 14<sup>th</sup> November 2019 which stated that:

a) The investment income budget for 2019/20 was £4m and is broadly on target:

b) From a benchmarking exercise, a total return of 1.6% was achieved for the reporting period, which was 0.46% above the average for similar Local Authorities return and 0.38% higher than the average return for all local authorities; and

c) the Prudential Indicators and Treasury Management indicators have been fully complied with.

### 3.10 **Treasury Management Strategy**

3.11 The Treasury Management Strategy Statement contained in Appendix A sets out the Council's proposed borrowing Strategy, in the context of the U.K.'s economic outlook, credit outlook and interest rate forecast as well as the local context of the requirement to borrow. Given the significant cuts to public expenditure and in particular to local government funding, the Authority's

borrowing strategy continues to address the key issue of affordability without compromising the longer-term stability of the debt portfolio.

- 3.12 The Council is undertaking a review of its borrowing strategy as set out in the TMSS, following the Capital Programme Review and the revised strategy will be reported to the Audit Committee
- 3.13 The Authority has previously raised the majority of its long-term borrowing from the PWLB but the government increased PWLB rates by 1% in October 2019 making it now a relatively expensive option. The Authority will now look to borrow any long-term loans from other sources including banks, pension funds and other local authorities, and will investigate the possibility of issuing bonds and similar instruments, in order to lower interest costs and reduce over-reliance on one source of funding in line with the CIPFA Code.
- 3.14 Alternatively, the Authority may arrange forward starting loans, where the interest rate is fixed in advance, but the cash is received in later years. This would enable certainty of cost to be achieved without suffering a cost of carry in the intervening period.
- 3.15 Any decisions will be reported to the appropriate decision making body at the next available opportunity. Please note that the borrowing of monies purely to lend on and make a return is unlawful and the Council will not engage in such activity.
- 3.16 Where spend is financed through the creation of debt, the Council is required to pay off an element of the accumulated capital spend each year. The payment is made through a revenue charge (the minimum revenue provision - MRP) made against the Council's expenditure, although it is also allowed to undertake additional voluntary payments if required (voluntary revenue provision - VRP). The MRP policy is set out in the TMSS which is contained in Appendix A.
- 3.17 The Council has chosen to adopt a Voluntary Revenue Provision (VRP) to be charged to the HRA This is in line with risks under consideration, the impact, and potential impact, on the Council's overall fiscal sustainability.
- 3.18 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. Both the CIPFA Code and the CLG Guidance require the Council to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Council's objective when investing money is to strike an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income. Where balances are expected to be invested for more than one year, the Council will aim to achieve a total return that is equal or higher than the prevailing rate of inflation, in order to maintain the spending power of the sum invested.

- 3.19 The investment strategy has been developed using the principle that the Council will also achieve optimum return on its investments commensurate with proper levels of security and liquidity. The Council's strategy is that given the risk and very low returns from short-term unsecured bank investments, the Authority will seek to explore new opportunities for further diversification into more secure and/or higher yielding asset classes during 2020/21. The majority of the Authority's surplus cash remains invested in short-term unsecured bank deposits, money market funds and local authority deposits.
- 3.20 The proposed structure for selecting counterparties is set out in the TMSS. The methodology has been proposed by Arlingclose Limited and after review, is being proposed to the Council for adoption. The Council has not listed all of the counterparties that meet these criteria in an appendix, as these counterparties will naturally change over time. The Council, in conjunction with its treasury management advisor, Arlingclose, will use Fitch, Moodys and Standard and Poor's ratings to derive its credit criteria. The Council's treasury adviser alerts officers to changes in ratings of all agencies.
- 3.21 The Corporate Director, Resources, has delegated responsibility to add or withdraw institutions from the counterparty list when circumstances change, either as advised by Arlingclose Limited (the Council's advisors) or from another reliable market source.

3.22 **Investment Strategy Report 2020/21**

- 3.23 The Investment Strategy Report is contained in Appendix B. This strategy meets the requirement of the Guidance issued by Government in January 2018 and sets out the Council's Strategy in relation to supporting local public services by lending to or buying shares in other organisations and earning investment income other than investment returns in cash balance (commercial investments). Members should note that as set out in section 3.5, the approved limit for charities' loans of £0.6m was exceeded by £0.4m in 2019/20, as the total approved limit did not take into account a pre-existing loan to one charity.

3.24 **Capital Strategy**

- 3.25 The capital strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of local public services along with an overview of how associated risk is managed and the implications for future financial sustainability. It has been written in an accessible style to enhance members' understanding of these sometimes technical areas.

3.26 Decisions made this year on capital and treasury management will have financial consequences for the Authority for many years into the future. They are, therefore, subject to both a national regulatory framework and to local policy framework, summarised in this report.

3.27 The Capital Strategy Report is contained in Appendix C. The Report sets out how the Capital Financing Requirement (CFR) for both the General Fund (GF) and the Housing Revenue Account (HRA) will change through to 2022/23, along with the Authorised Limit and the Operational Limit of borrowing and 10 Prudential Indicators (PIs). Any shortfall of resources results in a funding borrowing need.

### 3.28 **Other Treasury Management Issues**

3.29 To meet statutory requirements, clear delegated responsibility for overseeing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions. For this Council the delegated body is the Audit Committee. Officers will report details of the Council's treasury management activity to the Audit Committee at each of its meetings during the year. Additionally, a mid-year and full-year report will be presented to Full Council. set out in Appendices F and G

3.30 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. Training will be arranged as required and a training plan will be submitted to Audit Committee during 2020/21. The training needs of treasury management officers are periodically reviewed and form part of the annual learning and development plan for individual officers

## 4 **EQUALITIES IMPLICATIONS**

4.1 There are no equalities implications arising directly from this report

## 5 **OTHER STATUTORY IMPLICATIONS**

a. This section of the report is used to highlight further specific statutory implications that are either not covered in the main body of the report or are required to be highlighted to ensure decision makers give them proper consideration. Examples of other implications may be:

- Best Value Implications,
- Consultations,
- Environmental (including air quality),
- Risk Management,
- Crime Reduction,
- Safeguarding.
- Data Protection / Privacy Impact Assessment.

- b. **Best Value Implications:** The Treasury Management Strategy, Capital Strategy and Investment Strategy and the arrangements put in place to monitor them should ensure that the Council optimises the use of its monetary resources within the constraints placed on the Council by statute, appropriate management of risk and operational requirements. Assessment of value for money is achieved through monitoring against benchmarks and operating within budget.
  
- c. **Risk Management:** There is inevitably a degree of risk inherent in all treasury activity. The Investment Strategy identifies the risk associated with different classes of investment instruments and sets the parameters within which treasury activities can be undertaken and controls and processes appropriate for that risk. Treasury operations are undertaken by nominated officers within the parameters prescribed by the Treasury Management Policy Statement as approved by the Council. The Council is ultimately responsible for risk management in relation to its treasury activities. However, in determining the risk and appropriate controls to put in place the Council has obtained independent advice from Arlingclose whom specialise in Local Authority treasury issues.

## **6 COMMENTS OF THE CHIEF FINANCE OFFICER**

- 6.1 As this report is totally financial in nature it contains the comments of the Chief Financial Officer throughout the report. It contains the three strategy statements in relation to its treasury management arrangements.

## **7 LEGAL COMMENTS**

- 7.1 The Local Government Act 2003 ('the 2003 Act') provides a framework for the capital finance of local authorities. It provides a power to borrow and imposes a duty on local authorities to determine an affordable borrowing limit. It provides a power to invest. Fundamental to the operation of the scheme is an understanding that authorities will have regard to proper accounting practices recommended by the Chartered Institute of Public Finance and Accountancy (CIPFA) in carrying out capital finance functions.
  
- 7.2 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 ('the 2003 Regulations') require the Council to have regard to the CIPFA publication "Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes" ("the Treasury Management Code") in carrying out capital finance functions under the 2003 Act. If after having regard to the Treasury Management Code the Council wished not to follow it, there would need to be some good reason for such deviation.

- 7.3 It is a key principle of the Treasury Management Code that an authority should put in place “comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities”. Treasury management activities cover the management of the Council’s investments and cash flows, its banking, money market and capital market transactions, the effective control of risks associated with those activities and the pursuit of optimum performance consistent with those risks. It is consistent with the key principles expressed in the Treasury Management Code for the Council to adopt the strategies and policies proposed in the report.
- 7.4 The report proposes that the treasury management strategy will incorporate prudential indicators. The 2003 Regulations also requires the Council to have regard to the CIPFA publication “Prudential Code for Capital Finance in Local Authorities” (“the Prudential Code”) when carrying out its duty under the Act to determine an affordable borrowing limit. The Prudential Code specifies a minimum level of prudential indicators required to ensure affordability, sustainability and prudence. The report properly brings forward these matters for determination by the Council. If after having regard to the Prudential Code the Council wished not to follow it, there would need to be some good reason for such deviation.
- 7.5 The Local Government Act 2000 and regulations made under the Act provide that adoption of a plan or strategy for control of a local authority’s borrowing, investments or capital expenditure, or for determining the authority’s minimum revenue provision, is a matter that should not be the sole responsibility of the authority’s executive and, accordingly, it is appropriate for the Cabinet to agree these matters and for them to then be considered by Council.
- 7.6 The report sets out the recommendations of the Corporate Director Resources in relation to the Council’s minimum revenue provision, treasury management strategy and its annual investment strategy. The Corporate Director Resources has responsibility for overseeing the proper administration of the Council’s financial affairs, as required by section 151 of the Local Government Act 1972 and is the appropriate officer to advise in relation to these matters.
- 7.7 When considering its approach to the treasury management matters set out in the report, the Council must have due regard to the need to eliminate unlawful conduct under the Equality Act 2010, the need to advance equality of opportunity and the need to foster good relations between persons who share a protected characteristic and those who don’t (the public sector equality duty).

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## **Linked Reports, Appendices and Background Documents**

### **Linked Report**

- None

### **APPENDICES**

Appendix A – Treasury Management Strategy Statement

Appendix B - Investment Strategy Report

Appendix C - Capital Strategy Report

Appendix D – Prudential and Treasury Indicators

Appendix E – Treasury Management Policy Statement

Appendix F – Treasury Management Scheme of Delegation

Appendix G – Treasury Management Reporting Arrangement

Appendix H – Glossary

### **Background Documents – Local Authorities (Executive Arrangements)(Access to Information)(England) Regulations 2012**

- NONE

### **Officer contact details for documents:**

N/A