Non-Executive Report of the: **Audit Committee** 28th June 2017	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director of Resources	**Classification:** [Unrestricted or Exempt]
Treasury Management Outturn Report for 2016/17	

Originating Officer(s)	Bola Tobun, Investment & Treasury Manager
Wards affected	[All wards]

Summary

The Local Government Act 2003 requires that treasury management activities are reported to this Committee. This report summarises the Council's treasury management activities for the financial year ended 31 March 2017.

The report sets out the treasury management outturn position based on:

- the credit criteria adopted by the Corporate Director, Resources;
- the investment strategy for the financial year as approved by the Council; and
- the investment returns achieved.

The Council has complied with its legislative and regulatory requirements as set out in the legal comments at paragraph 5 of this report. The actual prudential and treasury management indicators for the year together with the comparators are also set out in this paper.

The Corporate Director, Resources confirms that;

- All treasury management activities were executed by authorised officers within the parameters agreed by the Council;
- All investments were made to counterparties on the Council's approved lending list and within limit; and
- No short-term or long-term borrowing was undertaken during the year to 31 March 2017. Note, £2.096m of a corporate capital scheme was financed internally without the need to raise new borrowing.

Long term debt reduced from £87.825m to £85.936m (excluding accrued interest shown in Statement of Accounts) as a result of loans maturing during the financial year.

The investment portfolio stood at £447.3m (excluding pension fund cash balances and accrued interest shown on the balance sheet) at 31 March 2017 with £15m being investments longer than one year. The Council earned 0.70% on short term lending, outperforming the benchmark of rolling average 7 Day LIBID rate of 0.20%.

The Council participates in a quarterly Investment Portfolio Benchmarking Analysis with 13 other local authorities and can demonstrate from this exercise that the risk and returns realised from investments are in line with the Council's risk appetite.

This report demonstrates that the Council is delivering its Treasury Management service in an open and transparent manner and that the Council is fulfilling its obligations under the Local Government Act 2003 to produce an annual review of activities. The report is being submitted to the Audit Committee to enable Members to fulfil their scrutiny role of the treasury management function as per CIPFA's Treasury Management Code of Practice. The report also provides information on the economic conditions prevailing in the final quarter of 2016-17.

Recommendations

Members are recommended to:

- Note the Treasury Management activities and performance against targets for the twelve months to 31 March 2017.
- Note the Pension Fund investments balance (set out in section 9 of Annex A).
- Note the Council's investments as at 31 March 2017 (as in Appendix 2 of Annex A).
- Note the Prudential indicators outturn for 2016/17 (set out in Appendix 1of Annex A).

1. REASONS FOR DECISIONS

1.1 This Council is required, by Regulations issued under the Local Government Act 2003, to produce an annual treasury report reviewing treasury management activities and the actual prudential and treasury indicators for 2016/17. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code).

1.2 The minimum reporting requirements stipulated by the Code are that full Council should receive the following reports:

- an annual treasury strategy in advance of the year(Council; 24 February 2016);
- a mid-year treasury update report (Council; 5 December 2016); and
- an annual report at the end of the year setting out the activity compared to the strategy (this report)

1.3 In addition, the Audit Committee received treasury management activity update reports on 28 June, 20 September, 8 November 2016 and 22 March 2017.

1.4 The Code requires Members to review and scrutinise treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

1.5 Presenting all of the above treasury management reports to the Audit Committee for scrutiny before they were reported to the full Council, fulfils the Council's requirements under the code of practice.

2. ALTERNATIVE OPTIONS

2.1 The Council is bound by legislation to have regard to the Treasury Management (TM) Code. The Code requires that the Council should receive an annual report on treasury management activities.

2.2 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 because of the requirements to ensure that Members are kept informed about treasury management activities and to ensure that these activities are in line with the investment strategy approved by the Council.

3. THE STRATEGY

3.1 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 require local authorities to have regard to the Treasury Management Code. The Treasury Management Code requires that the Council or a sub-committee of the Council should receive an annual report on treasury management activities.

3.2 The Council approved the Treasury Management Strategy Statement on 24 February 2016, which included the Investment Strategy, Minimum Revenue Provision and prudential indicators for 2016/17. These reports set out the parameters within which Treasury Management officers should operate when executing their roles. In line with the requirement of the Code, this report assists Members in discharging their responsibilities relating to the review and scrutiny of Treasury Management policies and activities in 2016/17.

3.3 The Council complied with its legislative and regulatory requirements in 2016/17 and was not in breach of any of the prudential and treasury management indicators. A more detailed report of the indicators is attached as Annex 1 with section 1 and 2 tables summarising the key indicators relating to capital expenditure activities in the year.

3.4 The Corporate Director, Resources also confirms that whilst the Council entered into a number of finance lease transactions during the year, the Council did not undertake any external borrowing during the year, thus operating within the authorised borrowing limit in the financial year.

3.5 The Council's actual capital expenditure was £61m less than the budgeted figure of £89.675m for the General Fund. Capital expenditure from the Housing Revenue Account (HRA) was £51.269m against a budget of £138.315m.

3.6 The HRA Capital Financing Requirements (CFR) increased from £75.583m to £84.269m for the year and General Fund CFR increased from £187.005m to £197.434m. The Council's overall CFR stood at £281.703m with total external debt (including PFI) of £121.192m at the end of this financial year 2016/17, giving a borrowing requirement of £160.511m. This borrowing need is being funded by internal borrowing, hence no external borrowing was undertaken during this financial year due to prevailing investment concerns of both counterparty risk and ultra-low investment returns.

3.7 The HRA does not receive a Minimum Revenue Provision (MRP) charge, with the exception of a MRP contained within finance leases. The statutory calculation of the MRP is applied to the General Fund; this is 4% of the aggregate assumed borrowing for general fund investment, known as the Capital Financing Requirement (CFR). The MRP applied to the General fund CFR for this financial year was £7.097m (including PFI and finance lease MRP).

3.8 No loan rescheduling was done during the year as the average 1% differential between PWLB new borrowing rates and premature repayment rates made rescheduling unviable.

3.9 The Council has continued with its conservative approach of prioritising security, appropriateness and liquidity over yield. Investments have therefore continued to be dominated by low counterparty risk considerations although this resulted in a high cost of carry as investment returns are relatively low compared to borrowing rate.

3.10 The strategy adopted in the original Treasury Management Strategy Report for 2016/17 approved by the Council on 24 February 2016 was subject to a revision during the year because of a large amount of cash balances and low investment rates as a consequence of the revision of the base rate from 0.50% to 0.25% after the E.U referendum. There was an amendment to the Council's Investment Strategy at the Full Council meeting in September 2016, to increase the monetary value from £50m to £100m for Long Term Investments and duration span from 3 year to 5 year limits.

3.11 The Council participates in a benchmarking club to enable officers to compare the Council's treasury management and investment returns against those of similar authorities. The model below shows the performance of benchmark club members, given the various levels of risks taken, as at 31 March 2017. The model takes into account a combination of credit, duration and returns achieved over the duration, and it includes data from 21 local authorities. Tower Hamlets lies close to the expected return given the Council's portfolio risk profile, which is placing deposits with institutions with the sovereign rate of AAA.

3.12 The comparison demonstrated that Tower Hamlets' investment portfolio had a lower credit risk of 2.77 compared to the benchmark group average of 3.19. (To measure the credit worthiness of a portfolio, a credit risk scale of 1-5 is applied, a portfolio with 5 will be the riskiest investment portfolio full of BBB+ and below credit rated institutions and a portfolio with 1 will be an investment portfolio full of institutions with credit rating AAA+).

3.13 The investment return associated with the level of risk taken on our investment portfolio is within the range 0.53% - 0.65% and the portfolio delivered 0.62%, which is 0.03% above its model portfolio.

3.14 The current institutions the Council can currently lend to, is as set out in Appendix 3 of Annex A.

4. COMMENTS OF THE CHIEF FINANCE OFFICER

4.1 This report fulfils the requirement to report the annual performance and position of the Council's Treasury and Investment activities to the Audit Committee and then Full Council. During 2016/17 the Council's investments portfolio delivered a return of 0.70%, which exceeded the benchmark average 7 days LIBID rate of 0.20% for the period.

4.2 For budgeting purposes, in 2016/17 the Council estimated that it would have an average cash balance of £300m during the year which it could invest to generate a 0.9% or £2.7m return on investment. However, the actual average balances for the year were significantly higher, totalling £404m. This was used to generate a 0.7% or £2.825m return on investment. The higher average cash balance was as a consequence of lower than expected capital expenditure during the year.

5. LEGAL COMMENTS

5.1 The Local Government Act 2003 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.

5.2 The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 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 Local Government Act 2003. 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.

5.3 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 review performance against the strategies and policies it has adopted.

5.4 The Treasury Management Code requires as a minimum that there be a practice of regular reporting on treasury management activities and risks to the responsible committee and that these should be scrutinised by that committee. Under the Council's Constitution, the audit committee has the functions of monitoring the Council's risk management arrangements and making arrangements for the proper administration of the Council's affairs and for the proper stewardship of public funds.

5.5 When discharging its treasury management functions, 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. Information is contained in section 15 of the report relevant to these considerations.

6. ONE TOWER HAMLETS CONSIDERATIONS

6.1 Interest income on the Council's cash flows has historically contributed significantly towards the budget. This Council's ability to deliver its various functions, to meet its Community Plan targets and to do so in accordance with its obligations under the Equality Act 2010 may thus be enhanced by sound treasury management.

7. BEST VALUE (BV) IMPLICATIONS

7.1 Assessment of value for money is achieved through:

- Monitoring against benchmarks
- Operating within budget

7.2 For example, investment returns exceeded the LIBID benchmark up to the end of March 2017 and the treasury function operated within budget for financial year 2016/17.

8. SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There are no Sustainable Actions for A Greener Environment implications.

9. RISK MANAGEMENT IMPLICATIONS

9.1 Any form of investment inevitably involves a degree of risk. To minimise risk the investment strategy has restricted exposure of council cash balances to UK backed banks or institutions with the highest short term rating or strong long term rating.

10. CRIME AND DISORDER REDUCTION IMPLICATIONS

10.1 There are no crime and disorder reduction implications arising from this report.

Linked Reports, Appendices and Background Documents

Linked Report
[None]

Appendices – contained in Annex A to this paper
Appendix 1: Prudential and Treasury Indicators
Appendix 2: Investments Outstanding as at 31st March 2017
Appendix 3: Counterparty List for London Borough of Tower Hamlets at 09/06/2017
Appendix 4: Definition of Fitch Credit Ratings
Appendix 5: Glossary

Local Government Act, 1972 Section 100D (As amended)
List of "Background Papers" used in the preparation of this report
Capita Treasury Advisory Services - Investment Reports & Benchmarking club report

Officer contact details for documents:

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