ANNEX 4

FULL COUNCIL **21st February 2018**	TOWER HAMLETS
Report of: Zena Cooke, Corporate Director Resources	**Classification:** Unrestricted
Treasury Management Strategy Statement For 2018-19	

Originating Officer(s)	Bola Tobun - Investment & Treasury Manager
Wards affected	All wards

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 CLG Guidance.

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 policy statement on the basis of which provision is to be made in the revenue accounts for the repayment of borrowing – Minimum Revenue Provision (MRP) Policy Statement;

    b) a Treasury Management Strategy Statement which sets out the Council's proposed borrowing for the financial year and establishes the parameters (prudential and treasury indicators) within which officers under delegated authority may undertake such activities; and

    c) an annual Investment Strategy which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.

3) This report also deals with the setting of Prudential Indicators for 2018-19, which ensure that the Council's capital investment decisions remain affordable, sustainable and prudent; the proposed indicators are detailed in Appendix 1. Under of the government's self-financing arrangements for the Housing Revenue Account (HRA) there are specific indicators relating to HRA capital investment.

4) The Department for Communities and Local Government (DCLG) issued revised Guidance on Local Authority Investments in March 2010 that requires the Authority to approve an investment strategy before the start of each financial year.

5) The Council adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the Authority to approve a treasury management strategy before the start of each financial year. CIPFA consulted on changes to the Code in 2017, but has yet to publish a revised Code. The Code as it requires the following:

a) Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities (Appendix 3);

b) Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives;

c) Approval by Full Council of Minimum Revenue Provision Policy, an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and prudential indicators for the year ahead together with arrangements for a Mid-year Review Report and an Annual Report covering activities during the previous year;

d) 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. The scheme of delegation for treasury management is shown in Appendix 4.

6) 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. More detailed reporting arrangements are shown in Appendix 5.

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 that the Full Council to:

i) Adopt the following policy and strategies:

   a) The Minimum Revenue Provision Policy Statement set out in section 2 at annex A attached to this report;

   b) The Treasury Management Strategy Statement set out in sections 5 & 6 at annex A attached to this report;

   c) The Annual Investment Strategy set out in section 7 at annex A attached to this report, which officers involved in treasury management, must then follow;

ii) Approve the prudential and treasury management indicators as set out in appendix 1 of annex A attached to this report.

iii) Delegate authority to Corporate Director, Resources

   - to amend prudential and treasury indicators, once capital expenditure forecast is firmed up.
   - use alternative forms of investment, such as pooled funds should the appropriate opportunity arise to use them, and should it be prudent and of advantage to the Council to do so.

1 REASONS FOR DECISIONS

1.1 It is consistent with the requirements of treasury management specified by CIPFA, to which the Council is required to have regard under the Local Government Act 2003 and regulations made under that Act, for the Council to produce three strategy statements to support the Prudential Indicators which ensure that the Council's capital investment plans are affordable, sustainable and prudent. The three documents that the Council should produce are:

- Minimum Revenue Provision Policy Statement
- Treasury Management Strategy, including prudential indicators
- Investment Strategy

2 ALTERNATIVE OPTIONS

2.1 The Council is bound by legislation to have regard to the CIPFA requirements for treasury management. 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.

2.2 The strategies and policy statement put forward in the report are considered the best methods of achieving the CIPFA requirements. Whilst it may be possible to adopt variations of the strategies and policy statement, this would risk failing to achieve the goals of affordability, sustainability and prudence.

3. BACKGROUND

3.1 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.

3.2 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 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.

3.3 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."

3.4 **REPORTING REQUIREMENTS** -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.

I. **A treasury management strategy statement** (this report) – it covers:
   - a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);

- the capital plans (including prudential indicators);
- the treasury management strategy (how the investments and borrowings are to be organised) including treasury indicators; and
- an investment strategy (the parameters on how investments are to be managed).

II. **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.

III. **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.

3.5 The Council uses Capita Asset Services, Treasury solutions as its external treasury management advisors. 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.

3.6 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.

The 2017/18 Strategy and Current Investment Position and Performance

3.7 The Strategy for 2017/18 was approved by Full Council in February 2017 and set the following objectives:-

a) The use of core cash for internal borrowing if not used for longer term investments.

b) The minimum Fitch credit ratings for the Council's investment policy:
   - Short Term: 'F1' the same criteria as last year
   - Long Term: 'A-' a notch down from 2016/17 criteria 'A'

c) The Council's budgeted investment return of £1.6m for 2017/18, with average rate of return 0.45% for average portfolio balances of £350m. Below table show the position of the investment income earned for this financial year to 31 December 2017.

Benchmark (Average 7 day LIBID)	Investment interest Earned	Average Cash Balance	Investment Interest Earned
0.23%	0.4%	£478m	£1.8m

d) The above budget was based on investing upto £100m for over 1 year duration in order to obtain a higher return, unfortunately longer term rates did not improve for the Council's acceptable minimum investment criteria.

e) Investments over 1 year is standing at £20m

f) The Council has not borrowed short or long term to date.

TREASURY MANAGEMENT STRATEGY FOR 2018/19

3.8 The strategy for 2018/19 covers two main areas:

Capital issues

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

Treasury management considerations:

- economic and interest rates forecast;
- the current treasury position;
- treasury indicators which limit the treasury risk and activities of the Council;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- the investment strategy;
- creditworthiness policy;
- service/policy investments.

3.9 The above elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, CLG MRP Guidance, the CIPFA Treasury Management Code and CLG Investment Guidance.

Developing the Strategy for 2018/19

3.10 In formulating and executing the strategy for 2018/19, the Council will continue to have regard for the DCLG's guidance on Local Government Investments and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectional Guidance Notes.

3.11 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.

3.12 The Council will also achieve optimum return on its investments commensurate with proper levels of security and liquidity. The borrowing of monies purely to on lend and make a return is unlawful and the Council will not engage in such activity.

3.13 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 alerted officers to changes in ratings of all agencies.

3.14 If a downgrade means the counterparty or investment fund no longer meets the Council's minimum criteria, its use for further investment will be withdrawn immediately. If funds are already invested with the downgraded institution, a decision will be made by the Corporate Director, Resources whether to withdraw the funds and potentially incur a penalty.

3.15 If an institution or fund is placed under negative rating watch (i.e. there is a probability of a rating change in the short term and the likelihood of that change being negative) and it is currently at the minimum acceptable rating for placing investments, no further investments will be made with that institution.

3.16 The Corporate Director, Resources has delegated responsibility to add or withdraw institutions from the counterparty list when ratings change, either as advised by Arlingclose Limited (the Council's advisors) or from another reliable market source.

3.17 The minimum Fitch credit ratings for the Council's investment policy for this financial year has changed, consideration not given to short term rating element and long term credit rating minimum criteria is the same as 2017/18:

- Long Term: 'A-'

3.18 Other market intelligence will also be used to determine institutions' credit worthiness, such as financial press, financial broker advice and treasury management meetings with other authorities, e.g. London Treasury Officers Forum. If this information shows a negative outcome, no further investments will be made with that body.

3.19 The strategy will permit the use of unrated building societies or challenger banks with assets in excess of £1.5bn for investment purposes.

3.20 The strategy proposes the continued use of core cash from £100m up to £150m to be held for longer term investment of over one year, if the interest rates are higher and appropriately reflect higher risk.

3.21 The cash balances, not immediately required to finance expenditure, are lent to the money market for the most appropriate periods as indicated by the cash flow model and current market and economic conditions;

a) Liquidity is maintained by the use of overnight deposits, MMF and call accounts;

b) The minimum amount of short-term cash balances required to support monthly cash flow management is £75 million;

c) The upper limit for investments longer than one year is £150 million;

d) The maximum period for longer term lending for banks, financial institutions and local authorities has been increased to 5 years;

e) All investment with institutions and investment schemes is undertaken in accordance with the Council's creditworthiness criteria as set out at section 7 of annex A attached to this report;

f) More cautious investment criteria are maintained during times of market uncertainty;

g) All investment with institutions and investment schemes is limited to the types of investment set out under the Council's approved "Specified" and "Non-Specified" Investments detailed at section 7 of annex A, and professional advice continues to be sought where appropriate;

h) All investment is managed within the Council's approved investment/asset class limits.

3.22 In light of the bail-in and ring fencing issues (please see below section 3.49 - 3.55 under other treasury management issues), the Corporate Director, Resources and her officers have been looking at investment funds as these are a step up from simple money market funds, where the fund manager takes a modest increase in credit and/or duration risk in order to deliver a modest increase in return. The advantages of investments funds are listed below:

- Potentially enhanced investment returns
- Diversifies opportunity and risk
- More appropriate to prevailing economic conditions
- Access to experienced fund managers and their resources
- Resource-efficient management

3.24 It is also worth noting that these funds operate on a Variable Net Asset Value (VNAV) basis, so there is no guarantee that the sale price will be equal to or above the purchase price, not all the funds have credit ratings, although the majority do.

3.25 Most of the funds offer distributing (i.e. income paying) share classes but some only offer accumulating.

3.26 Officers have been having meetings with the Council's treasury adviser to get our investments requirements right, as the volatility, investment returns and minimum investment periods differ from fund to fund.

Capital Programme and Prudential Borrowing

3.27 The table below summarises the capital expenditure plans and how these plans are being financed by capital or revenue resources. Any shortfall of resources results in a funding borrowing need.

Capital expenditure £m	**2016/17 Actual**	**2017/18 Revised Estimate**	**2018/19 Estimate**	**2019/20 Estimate**	**2020/21 Estimate**
General Fund	30.333	127.105	68.700	113.131	98.656
HRA	51.412	55.322	47.162	55.850	58.340
Total	**81.745**	**182.427**	**115.862**	**168.981**	**156.996**
Financed by:					
Grant	(31.591)	(23.576)	(8.270)	(11.920)	(9.259)
Major Repairs Allowance	(14.517)	(14.968)	(15.016)	(15.099)	(15.097)
Schools Contribution	0.000	(1.693)	0.000	0.000	0.000
Capital Receipts	(7.913)	(37.270)	(46.555)	(62.041)	(58.269)
S106 (Developers Contributions)	0.000	(29.735)	(13.067)	(22.192)	(14.861)
Revenue Financing	(25.627)	(34.432)	(12.929)	(15.329)	(11.966)
Total Financing Requirement	**(81.744)**	**(141.674)**	**(95.837)**	**(126.581)**	**(109.452)**
Prudential Borrowing	**2.097**	**40.753**	**20.025**	**42.400**	**47.545**

3.28 As part of the development of the prudential indicators attached as appendix 1 of annex A, which form part of the treasury management strategy, the Council must consider the affordability of its capital programme. In the past the programme has been financed by the use of capital resources such as receipts from asset sales and grants. The affordability of the programme is therefore calculated by the lost revenue income from the possible investment of the resources.

3.29 As shown in table above, there is a need to borrow up to £61m in total for 2018 to March 2019, £42m for 2019/20 and £47.5m for 2020/21 for the financing of capital expenditure as included in the current capital programme and the current prudential indicators. If the Council is to borrow, the affordability of the capital programme has been included in assessing the cost of borrowing along with the loss of investment income from the use of capital resources held in cash.

3.30 The current long term borrowing rate from the Public Works Loan Board is 2.93% for 25 years. Were the Council to temporarily borrow the necessary resources from its own cash balances rather than complete a further one year investment it would save the equivalent of 2.2% of the amount borrowed. The affordability of the capital programme has been calculated based upon the assumption that internal borrowing would occur initially.

3.31 The Council 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 from the Council's reserves, balances and cash flow has been used as a temporary measure. This strategy is prudent as investment returns are low and counterparty risk is still an issue that needs to be considered.

3.32 Under the circumstances and given the risks within the economic forecast, a prudent approach will be adopted with the 2018/19 treasury operations. The Corporate Director, Resources and her officers will monitor interest rates in financial markets and adopt a pragmatic approach to changing circumstances.

3.33 Should rates move quicker than the forecast predicts, the current and proposed strategies do allow the Corporate Director, Resources to take advantage of external borrowing. Any decisions will be reported to the appropriate decision making body at the next available opportunity.

3.34 The assumption is to borrow up to a maximum of £61m for 2018/19 and £42m for 2019/20, through the most economically advantageous method, as decided by the Corporate Director, Resources, from internal borrowing of core cash balances; PWLB loans; or other reputable sources of lending.

3.35 In summary the Council's borrowing strategy will give consideration to new borrowing in the following order of priority: -

a) The most cost effective borrowing will be internal borrowing by running down cash balances and foregoing interest earned at historically low rates. However, in view of the overall forecast for long term borrowing rates to increase over the next few years, consideration will also be given to weighing the short term advantage of internal borrowing against potential long term costs if the opportunity is missed for taking loans at long term rates which will be higher in future years.

b) Temporary borrowing from the money markets or other local authorities

c) PWLB variable rate loans for up to 10 years

d) Short dated borrowing from non PWLB below sources

e) Long term fixed rate market loans at rates significantly below PWLB rates for the equivalent maturity period (where available) and to maintaining an appropriate balance between PWLB and market debt in the debt portfolio.

f) PWLB borrowing for periods under 10 years where rates are expected to be significantly lower than rates for longer periods. This offers a range of options for new borrowing which will spread debt maturities away from a concentration in longer dated debt

3.36 The Council will continue to borrow in respect of the following:

a) Maturing debt (net of minimum revenue provision).

b) Approved unsupported (prudential) capital expenditure.

c) To finance cash flow in the short term.

Investment Strategy

3.37 The Council holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Authority's investment balance has ranged between £400m and £505m, and the levels are expected to reduce by £50m - £100m in the forthcoming year due to capital expenditure programme.

3.38 **Objectives:** 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.

3.39 **Negative interest rates:** If the UK enters into a recession in 2018/19, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

3.40 **Strategy:** Given the increasing risk and very low returns from short-term unsecured bank investments, the Council aims to diversify into more secure and/or higher yielding asset classes during 2018/19. This is especially the case for the estimated £150m that is available for longer-term investment. All of the Council's surplus cash is currently invested in short-term unsecured bank deposits, certificates of deposit and money market funds. This diversification will represent a substantial change in strategy over the coming year for the new strategy adopted in 2018/19.

Investment Return Budget to 2020/21

3.41 A cash flow projection up to March 2021 has been created reflecting the spending proposals in the Budget Strategy 2018/19 onwards. The cash flow projection and the interest rates forecast shows that anticipated investment income of £1.6m for 2017/18, based on average cash balance of £350m and average investment return of 0.45%. The anticipated investment income for 2018/19 is budgeted as £4.4m with average rate of 1.1% on cash balance of £400m, whereby £100m of core cash balances to be invested in pooled funds for over 3-5 years earning investment rate of 2% per annum. For 2019/20, £4.5m is the budgeted income, with average rate of 1.3% on average cash balance of £350m and for 2019/20; £4.5m is the budgeted income, with average rate of 1.5% on average cash balance of £300m. The Council may need to accept a higher level of risk in order to achieve these targets, whilst maintaining due regard for security of capital and liquidity.

Year-End	Estimated Average Cash Balance £m	Investment Income Forecast £m	Average Interest Rate
31st March 2019	400.00	4.40	1.10%
31st March 2020	350.00	4.50	1.30%
31st March 2021	300.00	4.50	1.5%

3.42 With reference to the proposal to use internal borrowing to finance the capital programme, as set out in the Capital Programme and Prudential Borrowing in annex A, the investment income suggested by the cash flow projection may be provided in part from internal charges or through the surplus generated by commercialisation projects.

Minimum Revenue Provision 2018/19

3.43 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 total debt is identified as the capital financing reserve and ensures that the Council includes external and internal borrowing along with other forms of financing considered to be equivalent to borrowing.

3.44 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).

3.45 It is recommended that because of budget constraints in the medium term the continue adoption of the existing statutory calculation which is based on 4% of the aggregate assumed borrowing for general fund capital investment - termed the Capital Financing requirement (CFR) as the basis of the Councils MRP relating to supported borrowing

3.46 The Council will use the asset life method for the calculation of the Minimum Revenue Provision on all future unsupported borrowing.

3.47 Based on the Council's latest estimate of its capital financing requirement, the budget for MRP for 2017/18 is £7.93m based on 2016/17 CFR of £281.703m and the budgeted MRP for 2018/19 is £7.92m based on estimated CFR for 2017/18 of £278.17m.

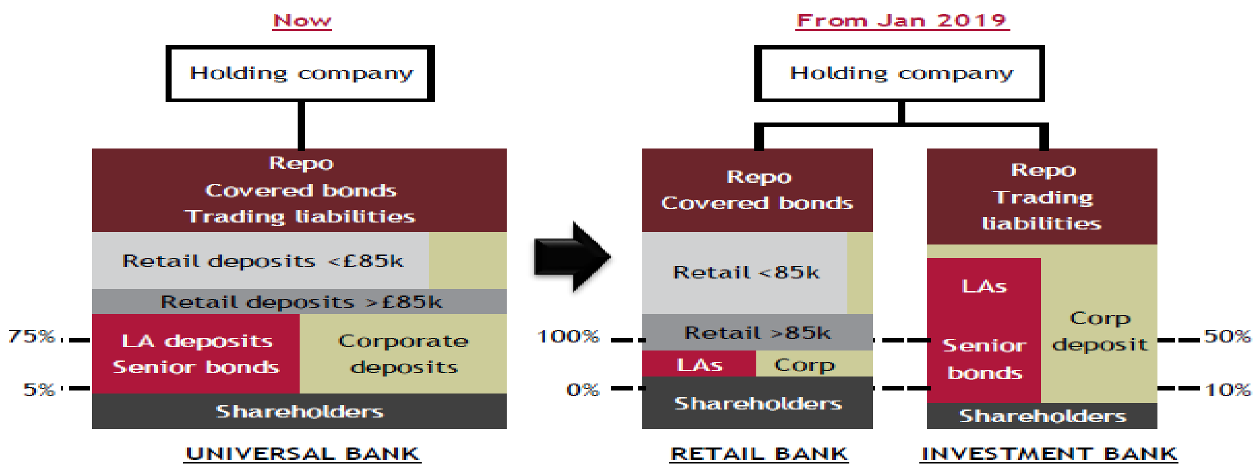
Other Treasury Management Issues

3.48 Further to implementation of MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE II (MiFID II), whereby the FCA has reclassified Local Authorities (LAs) as retail investors rather than the previous acquired professional status; this directive has been effective from 3 January 2018 and the Corporate Director, Resources has opted up as necessary with all our current counter parties, money market funds manager, advisers and brokers for the general treasury management functions.

Bail-in Issue

3.49 The failure of the banking system in a series of banking led crises that have stalked financial markets since the onset of the credit crunch in 2008. The new approach was the bail-in whereby a levy on the deposits would be made to lower the amount of the external bail-out. Initially, the levy would cover all bank deposits but it was revised, to apply to those with bank deposits in excess of £85k. This level reflects the extent of the current deposit guarantee limit in the Eurozone. The bail-in is the de facto solution to future bank problems across Europe including the UK. Hence term deposits with banks are riskier than before.

3.50 For professional investors, such as local authorities, the implications are that we will be the early contributors to a bail-in well before other retail depositors.



3.51 This follows that longer term deposits are even riskier because we are taking a credit view over the full term of the illiquid investment. So for bank deposits the risk is higher and yet returns are lower. This makes bank deposits an unsustainable mainstay of local authority investment activity.

UK Bank Ring-fencing

3.52 From January 2019 at the latest, the largest UK banks will be required to separate their retail banking services to individuals and small businesses from their investment banking activities. In practice this will only affect the big four banks (Barclays, Lloyds, HSBC and RBS), since other UK banks and building societies either only conduct retail banking activities or have less than £25 billion of Financial Services Compensation Scheme - covered deposits.

3.53 Barclays Bank, HSBC Bank and Royal Bank of Scotland intend to keep the existing legal entity as the non-ring-fenced “investment” bank, although RBS will be renamed NatWest Markets. Their ring-fenced “retail” banks will be called Barclays Bank UK, HSBC UK Bank and Royal Bank of Scotland respectively. The existing Lloyds Bank legal entity will become the retail bank, and a new investment will be created and named Lloyds Bank Capital Markets. NatWest Bank and Bank of Scotland will be ring-fenced “retail” banks.

3.54 If a UK bank experiences financial difficulties, “bail-in” arrangements will operate which will either reduce the value of deposits made or convert investments into shares. Based on the current understanding from the Council’s treasury management advisors, the probability of a bail-in is smaller at a retail bank, but the loss incurred would likely be a larger percentage of the investment deposited. This is because retail banks will typically have more capital to protect against losses, but fewer wholesale deposits and senior unsecured bonds to share losses with.

3.55 All UK banks with more than £25bn retail deposits are required to split into two banks by end 2018:

- A ring-fenced "retail" bank, providing basic services to individuals and SMEs
- A non-ring-fenced "investment" bank conducting higher risk activities

The law permits both banks to accept deposits from local authorities, Arlingclose expect bail-ins to be rarer, but larger, at retail banks than investment banks.

<u>Prudential Code</u>

3.56 The major change proposed is the introduction of a new report to full Council called the capital strategy, covering capital expenditure, investments, debt and other liabilities. It should be written at a relatively high level, suitable for all elected members to understand, and will include three prudential indicators – the authorised limit, the operational boundary and the capital expenditure total. Approval of the more technical detail, the remaining prudential indicators and the treasury management strategy can then be delegated to a committee where members with relevant skills or interests can take more time to properly approve the strategy and monitor the outcomes.

3.57 However, since government guidance still requires full Council to approve an investment strategy, MRP statement and (in Scotland) an annual report, CIPFA’s plans to reduce reporting to full Council.

<u>Treasury Management Code</u>

3.58 The main proposed change to the Code is to extend the definition of “investments” to include non-treasury investments held primarily for financial returns, such as investment property.

3.59 A new TMP 13 is introduced to note that risk management, governance and reporting procedures may be different for non-treasury investments. However, the objectives of security, liquidity and yield will apply to all investments.

3.60 Other proposed changes to the Treasury Management Code include:

a) Approval of the treasury management strategy may be delegated to a committee providing that full Council approves the capital strategy (see above under Prudential Code), although the clauses to be formally adopted in standing orders currently still require full Council to approve the strategy.

b) The inclusion of financial guarantees as instruments requiring risk management

c) Changing the investments over 364 days indicator to 365 days

d) Replacing the indicator on fixed and variable interest rates with a requirement to state how interest rate risk is managed

e) Extending the maturity profile indicator to include variable rate

IFRS 9 – From 2018/19 Classification of Financial Assets

3.61 Changes in fair value will impact revenue for:

- Structured loans and deposits where the cash flows are not solely payments of principal and interest (e.g. prepayment at par, credit-linked, equity-linked)
- Pooled funds and shares, unless an irrevocable option is taken to present fair value changes in unusable reserves (This option comes with significant new disclosures and so is only suitable for those investments that will be held for the long-term)

Impairment of Financial Assets

3.62 Expected 12 -month credit losses must be set aside and charged to revenue for most assets

a) Deposits, loans, bonds, lease and trade receivables

b) As little as 0.02% for an A-rated deposit

c) Maybe 3.8% for an average risk company loan

3.63 If credit risk increases significantly, then lifetime losses must be set aside, maybe 15% on a higher risk 5 year loan.

3.64 Amounts set aside are credited back to revenue if there is no default.

3.65 Impairments not applicable if non-contractual for example, Low Volatility Net Asset Value (LVNAV) Money Market Funds (MMFs), pooled funds and shares

4. COMMENTS OF THE CHIEF FINANCIAL OFFICER

4.1 The comments of the Corporate Director Resources are incorporated in the report

5. LEGAL COMMENTS

5.1 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.

5.2 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.

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 adopt the strategies and policies proposed in the report.

5.4 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.

5.5 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.

5.6 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.

5.7 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).

6 ONE TOWER HAMLETS CONSIDERATIONS

6.1 Capital investment will contribute to achievement of the corporate objectives, including all those relating to equalities and achieving One Tower Hamlets. Establishing the statutory policy statements required facilitates the capital investments and ensures that it is prudent.

7. BEST VALUE (BV) IMPLICATIONS

7.1 The Treasury Management 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.

7.2 Assessment of value for money is achieved through:

- Monitoring against benchmarks
- Operating within budget

8 SUSTAINABLE ACTION FOR A GREENER ENVIRONMENT

8.1 There are no sustainable actions for a greener environment implication.

9 RISK MANAGEMENT IMPLICATIONS

9.1 There is inevitably a degree of risk inherent in all treasury activity.

9.2 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.

9.3 Treasury operations are undertaken by nominated officers within the parameters prescribed by the Treasury Management Policy Statement as approved by the Council.

9.4 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 Capita Treasury Services who specialise in Council treasury issues.

10 CRIME AND DISORDER REDUCTION IMPLICATIONS

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

ANNEX & APPENDICES

ANNEX

Annex A – Treasury Management Strategy Statement (Working Document) for 2018-19

APPENDICES

Appendix A – Counter Party Credit Rating List

Appendix 1 – Prudential and Treasury Indicators

Appendix 2 – Definition of Fitch Credit Ratings

Appendix 3 – Treasury Management Policy Statement

Appendix 4 – Treasury Management Scheme of Delegation

Appendix 5 – Treasury Management Reporting Arrangement

Appendix 6 – Glossary

Local Government Act, 1972 Section 100D (As amended)

List of "Background Papers" used in the preparation of this report

Brief description of "background papers"	Name and telephone number of holder and address where open to inspection
	Bola Tobun, x4733, Mulberry Place