



CABINET REPORT

Report Title	TREASURY STRATEGY 2010-11 to 2012-13
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AGENDA STATUS: PUBLIC

Cabinet Meeting Date:	24 February 2010
Key Decision:	YES
Listed on Forward Plan:	YES
Within Policy:	YES
Policy Document:	YES
Directorate:	Finance and Support
Accountable Cabinet Member:	David Perkins
Ward(s)	Not Applicable

1. Purpose

The purpose of the report is to bring to Cabinet:

- An update to Financial Regulations in respect of the adoption of the revised CIPFA Treasury Management in the Public Services; Code of Practice and Cross Sectoral Guidance Notes (Fully revised second edition 2009)
- The Treasury Management Policy Statement
- The Treasury Management Practices (TMPs) and TMP Schedules for 2010-11
- The Treasury Strategy for 2010-11

2. Recommendations

2.1 That Cabinet recommend to Council that they approve:

- a) The adoption of the revised CIPFA Treasury Management in the Public Services; Code of Practice and Cross Sectoral Guidance Notes (Fully revised second edition 2009)
- b) The replacement of existing paragraph 5.9 of the Council's Financial Regulations with the wording at Annex A
- c) The Treasury Management Policy Statement at Annex B
- d) The Treasury Management Practices (TMPs) and TMP Schedules for 2010-11 at Annex C
- e) The Treasury Strategy for 2010-11 at Annex D, incorporating:
 - (i) The Capital Financing and Borrowing Strategy for 2010-11 including:
 - o The Council's policy on the making of Minimum Revenue Provision (MRP) for the repayment of debt, as required by the Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008.
 - o The Affordable Borrowing Limit for 2010-11 as required by the Local Government Act 2003.
 - (ii) The Investment Strategy for 2010-11 as required by the CLG (formerly ODPM) Guidance on Local Government Investments issued in 2004.

2.2 That Cabinet recommend to Council that they note:

- a) The proposed Debt Financing Budget 2010-11 to 2011-12 (paragraph 3.2.15 and Annex F).
- b) Adherence to the Council's policy on reserves and balances (paragraph 3.2.16).
- c) Compliance with the requirement under the Local Government Finance Act 1992 to produce a balanced budget (paragraph 3.2.17 & 3.2.18).

3. Issues and Choices

3.1 Report Background

Treasury Management in the Public Services - CIPFA Code of Practice

- 3.1.1 On 19 November 2007 the Council approved updated Financial Regulations, including at paragraph 5.9 the adoption of CIPFA's Treasury Management in the Public Services: Code of Practice (the Code), and the specific adoption of the key recommendations as described in Section 4 of that code.
- 3.1.2 In the light of the impacts on local authorities of the Icelandic bank situation in 2008, CIPFA has now published (in 2009) a fully revised second edition of the CIPFA Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes and a fully revised third edition of the Guidance Notes for Local Authorities.
- 3.1.3 It is a requirement of the Code that this Council should formally adopt the updated Code. Cabinet is asked to recommend to Council that they adopt the revised Code as set out at Annex A, replacing paragraph 5.9 of the existing Financial Regulations.
- 3.1.4 Officers have prepared this report and the accompanying annexes to incorporate the requirements of the updated code throughout.

CIPFA Prudential Code for Capital Finance in Local Authorities

- 3.1.5 The CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code), published in October 2003, introduced enhanced requirements for the manner in which capital spending plans should be considered and approved, and in conjunction with this, the requirement for an integrated treasury management strategy.
- 3.1.6 The Prudential Code requires the Council to set a range of prudential indicators for capital finance and a report setting out the prudential indicators for 2010-11 to 2012-13 is included elsewhere on this agenda.
- 3.1.7 CIPFA has issued a revised Prudential Code in 2009. Three of the existing prudential indicators have now been re-classified as treasury indicators, and these are included in this report:
- Authorised limit for external debt
 - Operational boundary for external debt
 - Actual external debt.
- 3.1.8 The code states that all the indicators are to be presented together as one suite. The Council's prudential and treasury indicators have all been set within an integrated strategy for capital expenditure and financing, and treasury management, and they are both brought to this same budget setting meeting for approval. The Council's Treasury Strategy includes both the prudential indicators relating to treasury and the treasury indicators.

- 3.1.9 The Prudential Code requires that where there is a significant difference between the net and the gross borrowing position, the risks and benefits associated with this strategy should be clearly stated in the annual strategy. This is covered in the Council's Treasury Strategy attached at Annex D at Section 9.

3.2 Issues

Economic Background

- 3.2.1 The UK, along with most major world economies, began 2009 in recession following the worldwide banking crisis of 2008. Banks were reluctant to lend due to fears over their weakened balance sheets, and many governments were forced to rescue their major banks in order to prevent the collapse of the world banking system. Central bank rates were cut in an attempt to counter the recession; the UK bank base rate was cut to 0.5% in March 2009 and has remained at this level throughout the year.
- 3.2.2 Worldwide, government debt increased as more support was given to failing banks, and the sovereign ratings of several countries were downgraded due to weak growth and increased debt. Standard and Poor's placed the UK's sovereign rating on negative outlook in May 2009, following concerns that UK government debt could approach 100% of GDP. The credit ratings of many worldwide banks continued to be unstable throughout the year, and while the frequency of downgrades has now decreased, negative rating watches remain in place for many counterparties.
- 3.2.3 While economic growth returned in the US and the EU in the third quarter of 2009, recovery in the UK has been slower, and the recession continued until January 2010. When the UK finally came out of recession, the level of growth was disappointing, at just 0.1%.
- 3.2.4 Opinion is divided on the speed and strength of recovery of the major world economies, and interest rate forecasts vary widely between analysts. In the UK the forthcoming general election is causing uncertainty for forecasters, but regardless of the outcome bank base rate is not expected to increase until the third quarter of 2010 at the earliest.

Local Impact

- 3.2.5 External events have continued to have a significant impact on the Council's debt financing budget. The low bank base rate led to an overall reduction in investment rates; in addition to this the reluctance of banks to lend money led to a lack of demand for funds, and those banks willing to accept deposits offered lower rates. As anticipated, rates of return on the Council's investments have fallen significantly throughout the year; the average monthly rate of return on investments fell from 3.05% to 1.04% between March and November, as investments placed before the banking crisis matured and the funds were reinvested at lower rates.
- 3.2.6 Following the collapse of the Icelandic banks in 2008, the Council's list of approved investment counterparties was severely restricted and the

maximum investment period shortened in order to safeguard investments. These changes led to decreased return on investments, as short term investment rates were significantly lower than longer term rates and the limited number of available investment counterparties led to more deposits being placed with the UK Debt Management Office, at rates below bank base rate.

- 3.2.7 In November 2009, following a period of increased stability of credit ratings, the maximum period for investments with counterparties on the Council's existing counterparty list was extended from 3 months to 12 months, subject to (a) the investment being within the Council's external treasury adviser's recommended time limit for the counterparty, and (b) that a maximum of £10m is invested in this way. £6m has now been invested for periods between 3 and 12 months, which has led to a slight increase in the monthly rate of return on investments.
- 3.2.8 The situation continues to be fluid, and it is essential to have a counterparty selection policy that can respond quickly to changes. A balanced view must be taken, but management of risk must take a higher priority over returns, so that the Council's balances are protected. Policies for the management of credit and counterparty risk are set out at Section 1 of TMP 1 (including the accompanying schedules), attached at Annex C. The Council's proposed approach for 2010-11 is set out at Section 18 of the Treasury Management Strategy attached at Annex D.

Treasury Management Policy Statement

- 3.2.9 The Council's Treasury Management Policy Statement is set out at Annex B. The statement follows the wording recommended by the revised CIPFA Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes.

Treasury Management Practices (TMPs)

- 3.2.10 The Council's Treasury Management Practices (TMPs) set out the manner in which the Council will seek to achieve its treasury management policies and objectives, and how it will manage and control those activities.
- 3.2.11 The TMPs are set out at Annex C, and are split as follows:
- Part 1: Main Principles
 - Part 2: Schedules
- 3.2.12 The Main Principles follow the wording recommended by the revised CIPFA Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes.
- 3.2.13 The Schedules cover the detail of how the Council will apply the Main Principles in carrying out its operational treasury activities.

Treasury Management Strategy 2010-11

3.2.14 The Council's Treasury Management Strategy for 2010-11 is set out at Annex D. The strategy incorporates:

(i) The Capital Financing and Borrowing Strategy for 2010-11 including:

- The Council's policy on the making of Minimum Revenue Provision (MRP) for the repayment of debt, as required by the Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008.
- The Affordable Borrowing Limit for 2010-11 as required by the Local Government Act 2003.

(ii) The Investment Strategy for 2010-11 as required by the CLG (formerly ODPM) Guidance on Local Government Investments issued in 2004. (Updated guidance is due to be published in 2010, with an implementation date of 1 April 2010)

Debt Financing Budget 2010-11 to 2012-13

3.2.15 The debt-financing budget has been prepared in accordance with the requirements of the relevant legislation and guidance and with full regard to the Council's proposed capital programme, treasury strategy and prudential indicators and is included in the Revenue Budget 2010-11 to 2012-13 report to Cabinet. A copy is attached at Annex F for information.

3.2.16 The debt financing budget has been prepared on the basis of the Council's policy on reserves and balances – i.e. to protect balances wherever possible to allow the option of supporting future years' budgets, aiming for a minimum level of unallocated general fund reserves of £2.195m at the end of 2010-11 having regard to the outcome of the financial risk assessment. This policy is included in the Revenue Budget 2010-11 to 2012-13 report to Cabinet and Council.

3.2.17 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from increases in interest charges caused by increased borrowing to finance additional capital expenditure, and any increases in running costs from new capital projects are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

3.2.18 The CIPFA Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes requires this report to include a reference to compliance under the Local Government Act 1992 to produce a balanced budget. Such compliance is demonstrated within the Revenue Budget 2010-11 to 2012-13 report to Cabinet & Council

Abbreviations

3.2.19 A list of abbreviations used in this report and the accompanying annexes is provided at Annex G.

3.3 Choices (Options)

3.3.1 Cabinet are asked to agree the recommendations at paragraph 2 above.

4. Implications (including financial implications)

4.1 Policy

4.1.1 The Treasury Strategy report sets the Council's policy on its debt and investment portfolios over the next financial year. It is revisited annually and reported to Cabinet and Council as part of the budget setting process.

4.2 Resources and Risk

4.2.1 The resources required to deliver the Council's treasury management strategy and policies over the next three years are incorporated into the Council's debt financing and debt management budgets, which are included in the Council's Revenue Budget 2010-11 to 2012-13 report to Cabinet & Council

4.2.2 Effective risk management is a fundamental requirement for the treasury management function, and this theme runs clearly throughout the Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes. The Council's Treasury Management Policy, Treasury Management Practices (TMPs) and Schedules, and Treasury Management Strategy for 2010-11 discuss the ways in which treasury management risk will be determined, managed and controlled.

4.2.3 The Council's appetite for risk must be clearly identified in its strategy report. The Treasury Strategy at Annex D affirms that priority will be given to the security of capital and liquidity when investing funds. This will be carried out by strict adherence to the risk management and control strategies set out in the Schedules to the Treasury Management Practices and the Treasury Management Strategy. Responsibility for risk management and control lie within the Council and cannot be delegated to an outside organisation.

4.2.4 Risks in the debt financing budget have been taken into account in earmarked reserves and in the Risk Assessment of General Fund Reserves

4.2.5 There is a risk that proposed changes to the arrangements for housing finance and the HRA subsidy mechanism could have a significant impact on the Council's capital financing and borrowing position at some point in the coming three-year period. The details, impacts and timing of such changes are not yet known, and a separate report will be brought to Cabinet (and Council if applicable) at a later date.

4.3 Legal

- 4.3.1 The Council is obliged to carry out its treasury management activities in line with statutory requirements and associated regulations and professional guidance. The relevant legislative and regulatory documents are referred to within the report and annexes and listed in the background papers.

4.4 Equality

- 4.4.1 An Equalities Impact Assessment has been carried out on the Council's Treasury Strategy for 2010-11, and the associated Treasury Management Practices (TMPs) and Schedules to the TMPs. This is attached at Annex H.
- 4.4.2 As a result of that assessment, it should be noted that the potential impact of the strategy and associated documents (including Treasury Management Practices (TMPs) and the Schedules to the TMPs) on the different equalities groups must be considered as it is developed and put together each year. This includes the consideration of the potential impact on the different equalities groups of any processes, procedures or outcomes arising from these.

4.5 Consultees (Internal and External)

- 4.5.1 Consultation on treasury management matters is undertaken as appropriate with the Council's external treasury advisers and with the Portfolio holder for Finance.

4.6 How the Proposals deliver Priority Outcomes

- 4.6.1 The Council is required to keep its treasury management strategy under review and monitor against it. The strategy reflects the requirements of the CIPFA Code of Practice for Treasury Management in the Public Services (Fully Revised Second Edition) 2009. This contributes positively to Comprehensive Area Assessment (CAA) Use of Resources requirements, and supports the Council's priority to be "an efficient well-managed organisation that puts our customers at the heart of what we do".

4.7 Other Implications

- 4.7.1 No other implications have been identified.

5. Background Papers

5.1.1 Statute, Regulation and Guidance

- CIPFA Treasury Management in the Public Services - Code of Practice and Cross-Sectoral Guidance Notes 2001
- Local Government Act 2003
- Local Authorities (Capital Finance and Accounting) (England) Regulations 2003
- CIPFA Prudential Code for Capital Finance in Local Authorities 2003
- ODPM Guidance on Local Government Investments 2004
- CIPFA Treasury Management in the Public Services - Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (Fully Revised Second Edition 2006)
- CIPFA Prudential Code for Capital Finance in Local Authorities – Fully Revised Guidance Notes for Practitioners 2007
- The Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008
- CIPFA Prudential Code for Capital Finance in Local Authorities (Fully Revised Second Edition) 2009
- CIPFA Treasury Management in the Public Services - Code of Practice and Cross-Sectoral Guidance Notes (Fully Revised Second Edition) 2009
- CIPFA Treasury Management in the Public Services - Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (Fully Revised Third Edition) 2009
- CLG Changes to the Capital Finance System – Consultation (November 2009)

5.1.2 Reports to Cabinet & Council

- Financial Regulations - Report to Council 19 November 2007 (Contains formal adoption of the CIPFA Code of Practice for Treasury Management)
- Capital Programme 2010-11 to 2012-13 - Report to Cabinet 24 February 2010
- Treasury Strategy 2010-11 to 2012-13 - Report to Cabinet 24 February 2010
- General Fund Revenue Budget 2010-13 - Report to Cabinet 24 February 2010
- Prudential Indicators for Capital Finance 2010-11 2012-13 - Report to Cabinet 24 February 2010

Bev Dixon, Finance Manager – Capital & Treasury, ext 7401