CAPITAL AND TREASURY MANAGEMENT STRATEGY 2018/19

1 INTRODUCTION

1.1 This report sets out the Council's Capital and Treasury Management Strategy for 2018/19 and seeks the views of the Review Committee on the approach proposed in this Strategy, before it is presented for approval by Full Council on 13 February 2018.

1.2 The Prudential Code for Capital Finance in Local Authorities (the Prudential Code) plays a key role in capital finance in local authorities, and it requires the Section 151 Officer to comment specifically on the Capital Strategy adopted by the Council. The full strategy is set out within this report.

1.3 Local authorities determine their own programmes for investment. The Prudential Code was developed by CIPFA as a professional code of practice to support local authorities in taking their decisions. Local authorities are required by regulation to have regard to the Prudential Code when carrying out their duties under Part 1 of the Local Government Act 2003. Part of the Prudential Code requires the Section 151 Officer to report explicitly on the affordability and risk associated with the Capital Strategy.

1.4 In financing capital expenditure, local authorities are governed by legislative frameworks, including the requirement to have regard to CIPFA's Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes.

1.5 In order to demonstrate that capital expenditure and investment decisions are taken in line with service objectives and properly take account of stewardship, value for money, prudence, sustainability and affordability, the Prudential Code requires authorities to have in place a Capital Strategy that sets out the long term context in which capital expenditure and investment decisions are made, and gives due consideration to both risk and reward and impact on the achievement of priority outcomes.

1.6 The Capital and Treasury Management Strategy provides an overview of the governance process for approval and monitoring of capital expenditure. It provides a projection of the Council's capital financing requirement and explains how the Council will make prudent revenue provision for the repayment of any debt.

1.7 The Council's approach to treasury management investment activities is set out at Section 8, and includes the criteria for determining how and where funds will be invested to ensure that the principal sums are safeguarded from loss and that sufficient liquidity is maintained to ensure that funds are available when needed. The treasury management investment strategy proposed for 2018/19 is consistent with that applied in previous years. The Council has a good track record with regard to its treasury investment activity, adhering to the statutory requirement to give priority to security and liquidity over yield. In addition, Internal Audit has issued a ‘good’ assurance opinion on the management of these activities, confirming that internal controls are consistently adhered to.

1.8 The Capital Strategy also sets out the Council’s policy approach to commercial investment activities, including processes, due diligence and defining the Council’s risk appetite in respect of these. The Council has not undertaken any commercial investment activities at the present time; however if this was to be considered in future it would be in accordance with the Council’s governance framework for decision making, and giving due regard to risk and proportionality. This section of the Capital Strategy may need to be revisited and updated once the revised statutory Guidance on Local Authority Investments is published and/or as the Council’s own agenda for commercial investments evolves.

1.9 The Council’s policies, objectives and approach to risk management of its treasury management activities, and the manner in which it seeks to achieve its policies and objectives for treasury management is set out in the Strategy, alongside the knowledge and skills available to the Council and provides confirmation that these are commensurate with the Council’s risk appetite.

1.10 The distinct, but inter-related, elements of the Capital Strategy therefore collectively demonstrate that the Council’s capital expenditure and investment decisions properly take account of stewardship, value for money, prudence, sustainability and affordability, by setting out the long term context in which capital expenditure and investment decisions are made, and by giving due consideration to both risk and reward and impact on the achievement of priority outcomes.

2 REPORTING

2.1 The Council is required to receive and approve, as a minimum, three main reports each year, which incorporate a variety of polices, estimates and actuals. These reports are:-

- The Capital and Treasury Management Strategy (this report), which covers:-
  - the capital plans (including prudential indicators);
  - a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
  - 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).

- The Mid Year Treasury Management Report which will update members with the progress of the capital position, amending prudential indicators as necessary, and whether the Treasury Strategy is delivering its objectives or whether any policies require revision. In addition, the Executive will receive quarterly updates of the capital programme position.

- Annual Strategy report (reported to Council in June). This provides details of actual performance compared to the estimates.

2.2 The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Review Committee.

3 CAPITAL AND TREASURY MANAGEMENT STRATEGY

3.1 The purpose of the Capital and Treasury Management Strategy is to demonstrate that the Council takes capital expenditure and investment decisions in line with service objectives and properly takes account of stewardship, value for money, prudence, sustainability and affordability. It sets out the long term context in which capital expenditure and investment decisions are made and gives due consideration to both risk and reward and impact on the achievement of priority outcomes. The Capital and Treasury Management Strategy comprises a number of distinct, but inter-related, elements as follows:

- Capital expenditure (see Section 4); which includes an overview of the governance process for approval and monitoring of capital expenditure, including the Council's policies on capitalisation, and an overview of its capital expenditure and financing plans.

- Capital financing and borrowing (see Section 5); provides a projection of the Council's capital financing requirement, how this will be funded and repaid. It therefore sets out the Council's borrowing strategy and explains how it will discharge its duty to make prudent revenue provision for the repayment of debt.

- Treasury management investments (see Section 8); explains the Council's approach to treasury management investment activities, including the criteria for determining how and where funds will be invested to ensure that the principal sums are safeguarded from loss and that sufficient liquidity is maintained to ensure that funds are available when needed.

- Commercial investments (see Section 11); provides an overview of those of the Council's policy on commercial investment activities that count as capital expenditure, including processes, due diligence and defining the Council's risk appetite in respect of these.

- Treasury management policy statement and practices (see Section 17); presents, for approval, updates to the Council's Treasury Management Policy Statement and to its Treasury Management Practices. These set out the Council's policies, objectives and approach to risk management of its treasury management activities, and the manner in which it seeks to achieve its policies and objectives for treasury management.

- Knowledge and skills (see Section 18); summarises the knowledge and skills available to the Council and provides confirmation that these are commensurate with the Council's risk appetite.

3.2 Further details are provided in the following sections.

4 CAPITAL EXPENDITURE

Capitalisation policies

4.1 Expenditure is classified as capital expenditure when it results in the acquisition or construction of an asset (e.g. land, buildings, roads and bridges, vehicles, plant and equipment etc.) that:

- Will be held for use in the delivery of services, for rental to others, or for administrative purposes; and
- Are of continuing benefit to the Council for a period extending beyond one financial year.
- Subsequent expenditure on existing assets is also classified as capital expenditure if these two criteria are met.

4.2 There may be instances where expenditure does not meet this definition but would nevertheless be treated as capital expenditure, including:

- Where the Council has no direct future control or benefit from the resulting assets, but would treat the expenditure as capital if it did control or benefit from the resulting assets; and
- Where statutory regulations require the Council to capitalise expenditure that would not otherwise have expenditure implications according to accounting rules.

Governance

4.3 The Section 151 Officer manages the preparation of a capital programme on an annual basis which is presented to Full Council for approval as part of the Medium Term Financial Strategy report.

4.4 Schemes will usually only be added to, or removed from, the capital programme as part of the annual budget setting process. Any request outside of this process to change the capital programme by adding or removing schemes, or by allocating additional scheme and payment approvals to an approved scheme, must be approved by Full Council in line with the Council's financial regulations.

4.5 The Section 151 Officer will also monitor performance against the Council's approved capital programme on an on-going basis, as part of the quarterly financial reports, which are presented to Executive by the Portfolio Holder for Finance. These financial overview reports will provide a comparison of the Council's projected expenditure with the latest approved capital programme.

Capital Expenditure Plans

4.6 The proposal is for capital investment of £1.210m for the 2018/19 programme,

4.7 When expenditure is classified as capital expenditure for capital financing purposes, this means that the Council is able to finance that expenditure from any of the following sources:

- Capital grants and contributions - amounts awarded to the Council in return for past or future compliance with certain stipulations.
- Capital receipts – amounts generated from the sale of assets and from the repayment of capital
- Loans, grants or other financial assistance.
- Revenue contributions – amounts set aside from the revenue budget
- Borrowing - amounts that the Council does not need to fund immediately from cash resources, but instead charges to the revenue budget over a number of years into the future. The implications of financing capital expenditure from borrowing are explained in Section 7.

5 CAPITAL FINANCING AND BORROWING

5.1 The Council's capital expenditure plans are one of the key drivers of treasury management activity. The capital expenditure plans are reflected in prudential indicators, which are designed to assist Members' overview and confirm capital expenditure plans.

Capital Expenditure and the Capital Financing Requirement.

5.2 This prudential Indicator is a summary of the Council's capital expenditure budget for 2018/19, subject to approval at Council on 13th February, both those agreed previously, and those forming part of this budget cycle. The table below also shows how these plans are being financed and any shortfall that will require borrowing. This table does not yet include capital expenditure for projects which have not yet been approved through the Investment Board. If required these will be considered during the year and the CFR will be updated accordingly, once the appropriate governance has been undertaken.

£000s	2016/17 Outturn	2017/18 Forecast	2018/19 Forecast	2019/20 Forecast	2020/21 Forecast
Opening CFR	**691**	**773**	**773**	**773**	**773**
Capital Expenditure	900	1,887	1,210	389	300
Financed by:					
Capital Finance reserve	500	230	796	389	300
Capital grants	250	375	408	-	-
Other Earmarked Reserves	-	620	-	-	-
Revenue Contribution	150	300	-	-	-
External Borrowing	-	-	-	-	-
Contribution from General Fund Reserve	-	362	-	-	-
Other	-	-	6	-	-
Closing CFR	**773**	**773**	**773**	**773**	**773**

5.3 The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need. Any capital expenditure above, which has not immediately been paid for, will increase the CFR. The CFR is reduced by the application of resources such as capital receipts, grants or charges to revenue.

Minimum Revenue Provision (MRP) Policy Statement

5.4 As noted above the Capital Financing Requirement (CFR) provides a measure of the amount of capital expenditure that the Council yet to fund from cash resources. Instead, the Council is required to set aside monies from the revenue budget each year to repay the borrowing. This practice is referred to as making minimum revenue provision (or MRP) for the repayment of debt. Statutory guidance requires MRP to be provided annually on a prudent basis, and interprets 'prudent' to mean that MRP charges on unsupported borrowing should be made over a period commensurate with the period the assets financed from borrowing continue to provide benefit. Where it is practical or appropriate to do so, the Council may make voluntary revenue provision, or apply capital receipts, to reduce debt over a shorter period.

5.5 Any future borrowing by the Council will require an MRP recognition through the revenue account, which will be considered as part of any future business case and the preferred method would be the Asset Life method (by way of either Equal Instalment or Annuity)

6 OTHER INDICATORS

The Use of the Council's Resources and the Investment Position

6.1 The application of resources (capital receipts, reserves etc) to either finance capital expenditure or other budget decisions to support the revenue budget will have an on-going impact on investments unless resources are supplemented each year from new sources (asset sales etc). Detailed below are estimates of the year end balances for each resource and anticipated day to day cash flow balances.

Year End Resources £000s	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Earmarked Reserves & General Fund Balance	6,317	7,284	8,184	9,084	9,984
Capital receipts reserve	1,185	389	-	-	-
Total core funds	**7,090**	**6,390**	**6,300**	**6,300**	**6,300**
Expected investments	**3,000**	**3,900**	**4,800**	**5,700**	**6,600**

Affordability Prudential Indicators

6.2 The previous sections cover the overall capital and control of borrowing prudential indicators, but within this framework prudential indicators are required to assess the affordability of the capital investment plans.

6.3 The indicators are designed to support and record local decision making in a manner that is publicly accountable but are not designed to be comparative performance indicators to other organisations. There are no recommended limits or values for the indicators.

6.4 These provide an indication of the impact of the capital investment plans on the Council's overall finances. Members are asked to approve the following indicators.

Ratio of financing costs to net revenue stream (revenue budget).

6.5 The table below shows the impact of borrowing compared to the general fund. It is negative because the Council does not currently borrow and so this represents only the interest received on investments as a comparison to the revenue budget.

%	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Ratio of Financing Costs to Net Revenue Stream	(0.40%)	(0.57%)	(0.79%)	(0.92%)	(1.03%)

6.6 **Incremental impact of capital investment decisions on the band D council tax.** If the capital programme is to be funded through revenue (council tax) this indicator identifies the revenue costs associated with proposed changes to the three year capital programme. The assumptions are based on the budget.

£000's	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Estimated Capital Expenditure	1,887	1,210	389	300	300
Incremental impact of capital investment	960	(677)	(821)	(89)	-
Estimated Council Tax Income	6,701	6,838	7,043	7,114	7,185
Council Tax – band D	0.14	(0.10)	(0.12)	(0.01)	-

7 BORROWING

7.1 Depending on the Council's Investment Board agreement to recommend particular business cases put forward for approval, it is possible that borrowing will be considered in future for larger capital schemes. However this will be considered on a case by case basis.

7.2 Borrowing could be used for "invest to save" projects providing the cost of servicing the debt is contained within the revenue savings/income the project generates, the project generates a positive net present value and the payback period for invest to save projects should be shorter than the life of the asset.

7.3 The following issues will be considered prior to undertaking any external borrowing:

- Affordability
- Maturity profile of existing debt
- Interest rate and refinancing risk
- Borrowing source including Internal

7.4 Sources of borrowing. In conjunction with advice from its treasury advisor, the council will keep under review the following external borrowing sources:

- Public Works Loan Board (PWLB) (or its replacement)
- any institution approved for investments
- any other bank or building society authorised to operate in the UK
- UK public and private sector pension funds (except for Essex Pension Fund)
- Capital market bond investors
- Municipal Bonds Agency - created to enable local authority bond issues
- Capital markets (stock issues, commercial paper and bills)

7.5 Borrowing would add pressure on the revenue budget as MRP and interest would become payable. The capacity to make these payments would need to be identified in advance, to ensure they are affordable.

7.6 Where capital expenditure on an asset is financed wholly or partly by borrowing or credit arrangements, MRP is to be determined by reference to the life of the asset. With the Equal Instalment approach, MRP is determined by reference to the life of the asset and an equal amount charged in each year. The Annuity method involves a more complex calculation. Here, MRP is the principal element for the year of the annuity required to repay over the asset life the amount of capital expenditure financed by borrowing.

8 TREASURY MANAGEMENT

8.1 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 initially before considering investment return.

8.2 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.

8.3 The investment policy objective for this Council is the prudent investment of its treasury balances. The Council's investment priorities are <u>security</u> of capital and liquidity of its investments so that funds are available for expenditure when needed.

8.4 Both the CIPFA Code and the DCLG 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 generation of investment income to support the Council's spending plans is an important, but secondary objective.

8.5 The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

8.6 The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

TREASURY INDICATORS: LIMITS TO BORROWING ACTIVITY

The Operational Boundary

8.7 This is the limit beyond which external debt is not normally expected to exceed. In most cases, this would be a similar figure to the CFR, limited to 85% of the closing CFR.

8.8 The Operational Boundary reflects the most likely (not worst case scenario), and should be a prudent view of the level of gross external indebtedness (borrowing + long term liabilities). It is regularly monitored and any breaches would be investigated promptly.

The Authorised Limit for external debt.

8.9 A further key prudential indicator represents a control on the maximum level of borrowing. This represents the upper limit beyond which external debt is prohibited, and this limit can only be revised by Full Council. It reflects the level of external debt which could be afforded in the short term, but is not sustainable in the longer term and provides headroom over and above the operational boundary which should be sufficient for unusual cash limits.

8.10 This is the statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all councils' plans, or those of a specific council, although this power has not yet been exercised.

The Authorised and Operational limits are based on the assumption that there will be long term borrowing to fund capital expenditure and that borrowing will be to fund long and short term cash flow requirements. The limits include balance sheet liabilities such as finance leases and creditors.

Authorised limit £000s	2017/18 Estimate	2018/19 Estimate	2019/20 Estimate	2020/21 Estimate	2021/22 Estimate
Debt	800	800	800	800	800

Treasury Management Limits on Activity

8.11 There are debt related treasury activity limits. The purpose of these are to restrain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of any adverse movement in interest rates. However, if these are set to be too restrictive they will impair the opportunities to reduce costs / improve performance.

8.12 The limit indicators are shown separately for borrowing and investments. Fixed rates for investments or borrowing for a period of less than one year are treated as variable by the Prudential Code.

Interest rate Exposures %	2018/19	2019/20	2020/21
	Upper	**Upper**	**Upper**
Limits on fixed interest rates:			
Borrowing	75	75	75
Investments	25	25	25
Limits on variable interest rates:			
Borrowing	25	25	25
Investment	75	75	75

9 BORROWING IN ADVANCE OF NEED

9.1 The Council has some flexibility to borrow funds for use in future years where a future need for borrowing has been identified. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Council can ensure the security of such funds.

9.2 The Section 151 Officer may do this under delegated power where, for instance, a sharp rise in interest rates is expected, and so borrowing early at fixed interest rates will be economically beneficial or meet budgetary constraints. Whilst the Section 151 Officer will adopt a cautious approach to any such borrowing, where there is a clear business case for doing so borrowing may be undertaken to fund the approved capital programme or to fund future debt maturities.

9.3 In determining whether borrowing will be undertaken in advance of need the Council will:

– Revenue liabilities created, and the implications for the future plans and budgets have been considered;

– Economic and market factors that might influence the manner and timing of any decision to borrow;

– Consider the merits and demerits of alternative forms of funding; and

– Consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use

9.4 Borrowing in advance will be made within the constraints that:

– It will be limited to no more than 50% of any expected increase in borrowing need (CFR) over the three year planning period; and

– Would not look to borrow more than 2 years in advance of need.

9.5 Risks associated with any advance borrowing activity will be subject to appraisal in advance and subsequent reporting through the mid-year or annual reporting mechanism. It is unlikely that the Council will require any borrowing in advance of need.

10 ANNUAL INVESTMENT STRATEGY

10.1 The Council has no plans to deviate from its current investment strategy for Treasury Management investments. A full list of those items included in the 2018/19 strategy are:

- Term and Call Deposits with banks and building societies
- Term deposits, call deposits and bonds with other UK Local Authorities
- Certificates of deposit with banks and building societies
- Deposit Facility
- Money Market funds (both Standard and Enhanced)
- Debt Management Agency Deposit Facility (Government Managed)
- Treasury Bills

11 COMMERCIAL INVESTMENTS

11.1 The prolonged low interest rate environment has meant that treasury management investments have not generated significant returns. However, the introduction of the general power of competence has given local authorities far more flexibility in the types of activity they can engage in. These changes in the economic and regulatory landscape, combined with significant financial challenges, have led many authorities to consider different and more innovative types of investment.

11.2 CIPFA recently issued an update to its Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes (the Treasury Management Code). One of the main changes introduced by the new Code is to require authorities to incorporate all of the financial and non financial assets held for financial return in authorities' annual capital strategies.

11.3 Separately, the Department for Communities and Local Government has recently consulted on changes to its statutory Guidance on Local Authority Investments. At the time of writing this strategy, the revised statutory guidance had not been issued, but it is expected that the guidance will reinforce the need for commercial investment activity to be included in the annual Capital Strategy.

11.4 In advance of confirmation of the statutory requirements related to commercial investment activities, the following paragraphs provide an overview of the Council's current approach to commercial investment activity. This section of the Capital Strategy will need to be updated once the revised statutory Guidance on Local Authority Investments is published and/or as any plans for the Council's own commercial investments evolves.

11.5 It is worth highlighting that any commercial investment activities are subject to approval in accordance with the Council's governance framework for decision making.

Commercial investment objectives

11.6 The Council does not currently hold any investments for non Treasury Management purposes. If at a future date the Council were to consider this option the primary objectives of any commercial investment activities would be:

- **Security** – to protect the capital sums invested from loss; and
- **Liquidity** – ensuring the funds invested are available for expenditure when needed.

11.7 The generation of yield is distinct from these prudential objectives. However, once proper levels of security and liquidity are determined, it is then reasonable to consider what yield can be obtained consistent with these priorities.

11.8 Non-core activities and investments could be undertaken by the Council, subject to the appropriate governance, in order to generate income to support the delivery of a balanced budget. Such investments would only be entered into following a full assessment of the risks and having secured expert external advice (i.e. where it is relevant to do so).

Loans to Subsidiaries

11.9 Loans to subsidiaries may be considered, as part of a wider strategy for local economic growth, even though they may not all be seen as prudent if adopting a narrow definition of prioritising security and liquidity.

11.10 Such loans will be considered when all of the following criteria are satisfied:

- The loan is given towards expenditure which would, if incurred by the Council, be capital expenditure;
- The purpose for which the loan is given is consistent with the Council's corporate / strategic objectives and priorities;
- Due diligence is carried out that confirms the Council's legal powers to make the loan, and that assesses the risk of loss over the loan term;
- A formal loan agreement is put in place which stipulates the loan period, repayment terms and loan rate (which will be set at a level that seeks to mitigate any perceived risks of a loss being charged to the General Fund, and takes appropriate account of state aid rules) and any other terms that will protect the Council from loss;

Other commercial investments

11.11 The Capital Strategy will be updated should any commercial investment opportunities be agreed during 2018/19 and/or in the event that the statutory Guidance on Local Authority Investments, when issued, requires further content to be included.

12 CREDIT RATINGS

12.1 This Council applies the creditworthiness service provided by Link Asset Services. This service employs a sophisticated modelling approach utilising credit ratings from the three main credit rating agencies - Fitch, Moody's and Standard & Poor's. The credit ratings of counterparties are supplemented with the following overlays:

- credit watches and credit outlooks from credit rating agencies;
- CDS spreads to give early warning of likely changes in credit ratings;
- sovereign ratings to select counterparties from only the most creditworthy countries.

12.2 This modelling approach combines credit ratings, credit Watches and credit Outlooks in a weighted scoring system which is then combined with an overlay of CDS spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. These colour codes are used by the Council to determine the suggested duration for investments. The Council will therefore use counterparties within the following durational bands

Capita Colour Coding	Maximum Duration	Maximum Investment
No colour	Not to be used	0
Green	100 days	£6m
Red	6 months 100 days	£3m £6m
Orange	1 year 6 months 100 days	£1m £3m £6m
Blue	1 year 1 year 6 months 100 days	£4m £3m £3m £6m
Purple	2 years 1 year 1 year 6 months 100 days	£3m £4m £3m £3m £6m

Organisation	Maximum Duration	Maximum Investment
Debt Management Office (Government Body)	6 months	£14m
Lloyds Bank current account The Council's main banker	On call (can be withdrawn immediately)	£5m
Money Market Funds – AAA long-term credit rating	On call (can be withdrawn immediately)	£5m per fund
Certificates of Deposit and Treasury Bills.	Will follow the Capita Colour Coding limits as per the above table.	Will follow the Capita Colour Coding limits as per the above table.
Local Authorities	1 year	£3m
Municipal Bonds Agency	10 years	£10,000 & 0.6% of borrowing

12.3 The Link Asset Services' creditworthiness service uses a wider array of information other than just primary ratings. Furthermore, by using a risk weighted scoring system, it does not give undue preponderance to just one agency's ratings.

12.4 Typically the minimum credit ratings criteria the Council use will be a Short Term rating (Fitch or equivalents) of F1 and a Long Term rating of A-. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.

12.5 All credit ratings will be monitored weekly. The Council is alerted to changes in ratings of all three agencies through its use of Link Asset Services creditworthiness service. If a downgrade results in the counterparty / investment scheme no longer meeting the Council’s minimum criteria, its further use as a new investment will be withdrawn immediately. In addition to the use of credit ratings the Council will be advised of information in movements in credit default swap spreads against the iTraxx benchmark and other market data on a daily basis via its Passport website, provided exclusively to it by Link Asset Services. Extreme market movements may result in downgrade of an institution or removal from the Council’s lending list.

12.6 Sole reliance will not be placed on the use of this external service. In addition this Council will also use market data and market information, information on any external support for banks to help support its decision making process

Country Limits

12.7 The Council has determined that it will only use approved counterparties from countries with a minimum sovereign credit rating of AA+ from Fitch Ratings (or equivalent from other agencies if Fitch does not provide).

12.8 Following the vote to leave the European Union, the United Kingdom’s credit rating dropped to AA from AA+. Upon discussion with our Treasury Management advisers, Link Asset Services Ltd, the approval to remove the United Kingdom from this stipulation of credit rating criteria was granted at Full Council 19 July 2016. Capita has advised that it would be very unlikely for a UK institution to be allowed to default, given the Government’s robust financial backing and the consequences this might have on the industry as a whole.

12.9 Countries other than the UK will be subject to a £3m investment limit for duration of up to one year, subject to Section 151 Officer authorisation.

12.10 Those countries that have a sovereign rating of AA+ or higher currently are:

AAA

- Australia
- Canada
- Denmark

- Germany
- Luxembourg
- Netherlands
- Norway
- Singapore
- Sweden
- Switzerland

AA+

- Finland
- Hong Kong
- USA

AA

- United Kingdom

Investment Management

12.11 The Council does not use a fund manager and funds are managed in-house. Investments will accordingly be made with reference to the core balances and cash flow requirements and the outlook for short-term interest rates (i.e. rates for investments up to 12 months).

12.12 **Investment returns expectations.** Bank Rate is forecast to stay flat at 0.50% until quarter 4 of 2018/19 and not rise above 1.25% by quarter 1 2020/21. Bank Rate forecasts for financial year ends (March) are:-

- 2017/ 2018 0.50%
- 2018/ 2019 0.75%
- 2019/ 2020 1.00%
- 2020/ 2021 1.25%

The suggested budgeted investment earnings rates for returns on investments placed for periods up to 100 days during each financial year are as follows:

- 2017/ 2018 0.40%
- 2018/ 2019 0.60%
- 2019/ 2020 0.90%
- 2020/ 2021 1.25%

12.13 There are upside risks to these forecasts (i.e. increases in Bank Rate occur sooner) if economic growth strengthens. However, should the pace of growth fall back there could be downside risk, particularly given the uncertainty over the final terms of Brexit. If growth expectations disappoint and inflationary pressures are minimal, any furtherany further increases in Bank rate could be pushed back.

12.14 It is expected that this authority will have sufficient funds to invest that will realise a return on investments c£50,000 for financial year 2018/19.

12.15 At the end of the financial year, the Council will report on its investment activity as part of its Annual Strategy Report.

13 MIFID II

13.1 Under new banking regulations (referred to as MiFID II) which took effect from 1 January 2018, all local authorities are classified as retail counterparties and will have to consider whether to opt up to professional status. This authority has met the criteria of opting up to professional status, enabling it to continue to invest in accordance with its Investment Strategy.

14 LIQUIDITY RISK MANAGEMENT

14.1 This council will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have sufficient liquidity in its investments, taking into account known and potential cash-flow requirements and the level of funds available to it which are necessary for the achievement of its business/service objectives.

14.2 Giving due consideration to the Council's level of balances over the next year, the need for liquidity, its spending commitments and provisioning for contingencies, it is considered very unlikely that the Council will have cash balances to invest other than on a temporary basis. For this reason, no cash will be held on term deposit maturities in excess of 1 year.

15 CASH AND CASH FLOW MANAGEMENT

15.1 The objective should be to keep low interest cash balances at an optimum and maximise temporary investments. There is likely to be a difference between forecast activity and actual activity and therefore working capital will need to be subject to regular review and report to Review Committee / Full Council in the light of changing levels of activity.

15.2 The council will prepare reports which include cash flow forecasts and actuals on a 12 month rolling basis so as to be able to determine:

- whether minimum acceptable levels of cash balances plus short-term investments might be (or have been) breached

– the adequacy (or otherwise) of standby/overdraft facilities or contingency arrangements

– the optimum arrangements to be made for investing and managing surplus cash.

16 SCHEME OF DELEGATION

16.1 Under the Code, the Council is required to specify its Scheme of Delegation for Treasury Management and the responsibilities of the Section 151 Officer, and this is shown below:-

(i) Full Council

- receiving and reviewing reports on treasury management policies, practices and activities.
- approval of annual strategy
- budget consideration and approval.
- receiving the end of year report on treasury management.

(ii) Review Committee Treasury Management Task & Finish Group

- scrutiny of the three main treasury reports, before recommendation to Council or Executive.

(iii) Executive

- approval of/amendments to the organisation's adopted clauses, treasury management policy statement and treasury management practices.
- approval of the division of responsibilities.
- receiving and reviewing regular monitoring reports and acting on recommendations.

(iv) Audit Committee

- reviewing the treasury management policy and procedures and making recommendations to the responsible body.

(v) Section 151 Officer

- recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance.
- submitting regular treasury management policy reports.
- submitting budgets and budget variations.
- receiving and reviewing management information reports.
- reviewing the performance of the treasury management function.

- ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function.
- ensuring the adequacy of internal audit, and liaising with external audit.
- Recommending the appointment of external service providers.

17 TREASURY MANAGEMENT POLICY STATEMENT AND TREASURY MANAGEMENT PRACTICES

17.1 During 2017, CIPFA consulted on proposed changes to its Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes (the Treasury Management Code), and published a revised version of the CIPFA Code in December 2017. The Treasury Management Code has largely been updated following recent developments in the marketplace and the introduction of the Localism Act 2011, which gave authorities greater flexibility to enter into a wider range of investment activities under the ‘general power of competence’.

17.2 The Treasury Management Code has a particular significance under the provisions of the Local Government Act 2003 which requires local authorities

‘*to have regard (a) to such guidance as the Secretary of State may issue, and (b) to such other guidance as the Secretary of State may by regulations specify*’.

17.3 The Treasury Management Code contains the following definition of treasury management activities which has been adopted by CIPFA:

The management of the organisation’s borrowing, investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.

This definition is intended to apply to all public service organisations in their use of capital and project financings, borrowings and all investments.

17.4 The updated Treasury Management Code clarifies that ‘investments’ in the above definition covers all of the Council’s financial assets, as well as other non-financial assets held primarily for financial returns if applicable. This means that it encompasses investments which are not managed as part of normal treasury management or under treasury management delegations.

17.5 The Treasury Management Code identifies three key principles for treasury management:

- Public service organisations should put in place formal and comprehensive objectives, policies and practices, strategies and reporting arrangements for the effective management and control of their treasury management activities.

- Their policies and practices should make clear that the effective management and control of risk are prime objectives of their treasury management activities and that responsibility for these lies clearly within their organisations. Their appetite for risk should form part of their annual strategy, including any use of financial instruments for the prudent management of those risks, and should ensure that priority is given to security and portfolio liquidity when investing treasury management funds.

- They should acknowledge that the pursuit of value for money in treasury management, and the use of suitable performance measures, are valid and important tools for responsible organisations to employ in support of their business and service objectives, and that within the context of effective risk management, their treasury management policies and practices should reflect this.

17.6 In accordance with these principles, the Council had previously adopted a Treasury Management Policy Statement, which set out the policies, objectives and approach to risk management of its treasury management activities, and a series of Treasury Management Practices (TMPs), which set out the manner in which the Council sought to achieve its policies and objectives for treasury management.

17.7 The Council's Treasury Management Policy Statement and its Treasury Management Practices have been updated to reflect the requirements of the updated Treasury Management Code. They are presented for approval in the following annexes:

- **Annex 1** – Treasury Management Policy Statement
- **Annex 2** – Treasury Management Practices
- **Annex 3** – Investment management practices for non treasury investments

18 KNOWLEDGE AND SKILLS

18.1 The Council recognises the importance of ensuring that all officers involved in the treasury management function (including commercial investment activities) are fully equipped to undertake the duties and responsibilities allocated to them. The Section 151 Officer is responsible for recommending and implementing the necessary arrangements and does this by:

- **Ensuring officers are both capable and experienced**. All individuals involved in the delivery of the treasury management function are required to undertake continuing professional development.

- **Providing training and technical guidance**

All individuals involved in the delivery of the treasury management function are provided with access to relevant technical guidance and training necessary to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills to undertake the duties and responsibilities allocated to them.

- **Appointing a treasury management and other professional advisors**
  By employing external providers of treasury management services, the Section 151 Officer ensures that the individuals involved in delivery of the Council's treasury management activities have access to specialist skills and resources.

18.2 Following a recent procurement process, the Council has been successful in securing the services of Link Asset Services "Link" (formerly Capita Asset Services) as its external treasury management advisors, entering into a 4 year contract.

18.3 The Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

It also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review.

18.4 The Section 151 Officer will ensure that elected members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities. Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

19 RISK IMPLICATIONS

19.1 As a debt free authority with a medium term resource strategy identifying the potential for investment income the Council's highest priority in its treasury management function is the security of those investments in accordance with the priorities set out in the CIPFA Code. Where investment returns are short term in nature they should be used to fund one-off expenditure or capital investment and not to balance the base revenue budget.

19.2 Sums are invested with a diversified range of counter parties using a wide range of instruments consistent with avoiding the risk of the capital sum being diminished through movements in prices.

19.3 This means that the Council whilst fundamentally risk adverse, will accept some modest degree of risk. It will consider first the range of risks and secondly how prudently to manage those different risks. It will ensure that priority is given to security and liquidity when investing funds before seeking to optimise yield. The use of different investment instruments and diversification of high credit quality counter parties along with country, sector and group limits, as set out in the Strategy, enables the Council to minimise the nature and extent of the different risks.

20 RESOURCE IMPLICATIONS

20.1 All interest paid and received is accounted for within the General Fund. The amount of income generated is dependent upon interest rates and level of balances.

21 LEGAL IMPLICATIONS

21.1 This strategy complies with the statutory requirements set out in the Local Government Act 2003 and associated guidance and regulations.

22 EQUALITY AND DIVERSITY IMPLICATIONS

22.1 None.

23 RECOMMENDATION

23.1 It is proposed that the Committee **RESOLVES**

(1) To note the Capital and Treasury Management Strategy Statement including the investment instruments, indicators, limits and delegations contained within the report.

(2) To note the Capital Expenditure Forecasts.

(3) To note the MRP policy for 2018/19.

(4) To note the Authorised Limit for external debt as laid down in the report.

(5) To note the updated Treasury Management Policy Statement and Treasury Management Practices at Appendices 1-3.

(6) To identify any issues on this topic for further consideration and discussion by the Committee.

(7) Recommend the contents of this report to Full Council.

Naomi Lucas

Naomi Lucas

Section 151 Officer

Background Papers:-

None.

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If you would like this report in large print, Braille or another language please contact 01702 318111.

Annex 1- Treasury Management Policy Statement

The following statement defines the policy and objectives of the Council's treasury management activities:

1. The Council defines its treasury management activities as:
    - The management of its 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.

2. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the Council.

3. The Council acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving value for money in treasury management, and of employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

4. The Council's policies for borrowing and investments will be set out within the annual Capital Strategy.

Annex 2 - Treasury Management Practices

TMP 1 - Risk Management General Statement

The Council regards a key objective of its treasury management activities to be the security of the principal sums it invests. Accordingly, it will ensure that robust due diligence procedures covering all external investment.

The Section 151 Officer will design, implement and monitor all arrangements for the identification, management and control of treasury management risk, will report at least annually on the adequacy/suitability thereof, and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the organisation's objectives in this respect, all in accordance with the procedures set out in TMP 6 Reporting requirements and management information arrangements.

In respect of each of the following risks, the arrangements which seek to ensure compliance with these objectives are set out in the schedule to this document.

[1] Credit and counterparty risk management

The Council will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with whom funds may be deposited, and will limit its investment activities to the instruments, methods and techniques referred to in

TMP4 Approved instruments, methods and techniques.
It also recognises the need to have, and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing arrangements.

[2] Liquidity risk management
The Council will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives. The Council will only borrow in advance of need where there is a clear business case for doing so and will only do so for the current capital programme or to finance future debt maturities.

[3] Interest rate risk management
The Council will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with

TMP6 Reporting requirements and management information arrangements.

It will achieve this by the prudent use of its approved instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates. This should be the subject to the consideration and, if required, approval of any policy or budgetary implications.

[4] Exchange rate risk management

It will manage its exposure to fluctuations in exchange rates so as to minimise any detrimental impact on its budgeted income/expenditure levels.

[5] Inflation risk management
The Council will keep under review the sensitivity of its treasury management assets and liabilities to inflation, and will seek to manage the risk accordingly in the context of its wider exposure to inflation.

[6] Refinancing risk management
The Council will ensure that its borrowing, private financing and partnership arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the organisation as can reasonably be achieved in the light of market conditions prevailing at the time.

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid overreliance on any one source of funding if this might jeopardise achievement of the above.

[7] Legal and regulatory risk management

The Council will ensure that all of its treasury management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counterparty policy under TMP1[1] credit and counterparty risk management, it will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged. The Council recognises that future legislative or regulatory changes may impact on its treasury management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the Council.

[8] Fraud, error and corruption and contingency management
The Council will ensure that it has identified the circumstances which may expose it to the risk of loss through fraud, error, corruption or other eventualities in its treasury management dealings. Accordingly, it will employ suitable systems and procedures, and will maintain effective contingency management arrangements, to these ends.

[9] Market risk management
The Council will seek to ensure that its stated treasury management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sum it invests, and will accordingly seek to protect itself from the effects of such fluctuations.

TMP 2 - Performance measurement
The Council is committed to the pursuit of value for money in its treasury management activities, and to the use of performance methodology in support of that aim, within the framework set out in its treasury management policy statement. Accordingly, the treasury management function will be the subject of ongoing analysis of the value it adds in support of the Council's business or service objectives and performance will be measured against relevant benchmarks.

TMP 3 - Decision-making and analysis
The Council will maintain full records of its treasury management decisions, and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time.

TMP 4 - Approved instruments, methods and techniques
The Council will undertake its treasury management activities by employing only those instruments, methods and techniques detailed in its annual Investments Strategy, and within the limits and parameters defined in TMP1 Risk management. The Council has reviewed its classification with financial institutions under MIFID II and will set out in its annual Investment Strategy those organisations with which it is registered as a professional client.

TMP 5 - Organisation, clarity and segregation of responsibilities, and dealing arrangements
The Council considers it essential, for the purposes of the effective control and monitoring of its treasury management activities, for the reduction of the risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times a clarity of treasury management responsibilities. The principle on which this will be based is a clear distinction between those charged with setting treasury management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of treasury management decisions, and the audit and review of the treasury management function. If and when it is intended, as a result of lack of resources or other circumstances, to depart from these principles, the Section 151 Officer will ensure that the reasons are properly reported in accordance with TMP6 Reporting requirements and management information arrangements, and the implications properly considered and evaluated. The Section 151 Officer will ensure that there are clear written statements of the responsibilities for each post engaged in treasury management, and the arrangements for absence cover. The Section 151 Officer will also ensure that at all times those engaged in treasury management will follow the policies and procedures set out. The Section 151 Officer will ensure there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds. The delegations to the Section 151 Officer in respect of treasury management are set out in the Council's Financial Regulations and Scheme of Delegation for Financial Management. The Section 151 Officer will

fulfil all such responsibilities in accordance with the Council's policy statement and TMPs and the CIPFA Standard of Professional Practice on Treasury Management.

TMP 6 - Reporting requirements and management information arrangements
The Council will ensure that regular reports are prepared and considered on the implementation of its treasury management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; on the implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its treasury management activities; and on the performance of the treasury management function.

As a minimum:

- Full Council will receive an annual report on the strategy and plan to be pursued in the coming year.
- The Executive will receive reports on the performance of the treasury management function, and on any circumstances of non-compliance with the Council's Treasury Management Policy Statement and TMP's, as part of the Council's quarterly financial overview reporting.

The Council's Review Committee has responsibility for the scrutiny of treasury management policies and practices.

TMP 7 - Budgeting, accounting and audit arrangements
The Section 151 Officer will prepare, and full Council will approve and, if necessary, from time to time will amend, an annual budget for treasury management, which will bring together all of the costs involved in running the treasury management function, together with associated income. The matters to be included in the budget will at minimum be those required by statute or regulation, together with such information as will demonstrate compliance with TMP1 Risk management, TMP 2 Performance Measurement, and TMP 4 Approved instruments, methods and techniques. The Section 151 Officer will exercise effective controls over this budget, and will report upon and recommend any changes required in accordance with TMP 6 Reporting requirements and management information arrangements. The Council will account for its treasury management activities, for decisions made and transactions executed, in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

TMP 8 - Cash and cash flow management
Unless statutory or regulatory requirements demand otherwise, all monies in the hands of the Council will be under the control of the Section 151 Officer, and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis, and the Section 151 Officer will ensure that these are adequate for the purposes of monitoring compliance with TMP1[1] liquidity risk management. TMP 9 – Money laundering. The Council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. Accordingly, it will maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that staff involved in this are properly trained.

The present arrangements, including the name of the officer to whom reports should be made, are detailed in the Council's Anti-Money Laundering Policy.

TMP 10 - Training and qualifications

The Council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced, and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The responsible officer will recommend and implement the necessary arrangements. The responsible officer will ensure that elected members tasked with treasury management responsibilities, including those responsible for scrutiny, have access to training relevant to their needs and those responsibilities.Those charged with governance recognise their individual responsibility to ensure that they have the necessary skills to complete their role effectively.

TMP 11 - Use of external service providers

The Council recognises that responsibility for treasury management decisions remains with the Council at all times. However, the Council recognises that there may be value in employing external providers of treasury management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will do so following a full evaluation of the costs and benefits, and will also ensure that the terms of their appointment are properly agreed and documented, and subjected to regular review. Where services are subject to formal tender or re-tender arrangements, legislative requirements will always be observed. The monitoring of such arrangements rests with the Section 151 Officer.

TMP 12 - Corporate governance

The Council is committed to the pursuit of proper corporate governance throughout its businesses and services, and to establishing the principles and practices by which this can be achieved. Accordingly, the treasury management function and its activities will be undertaken with openness and transparency, honesty, integrity and accountability.

This organisation has adopted and has implemented the key principles of the CIPFA Treasury Management in the Public Services Code of Practice and Cross Sectoral Guidance Notes. This, together with the other arrangements detailed in the schedule to this document, are considered vital to the achievement of proper corporate governance in treasury management, and the responsible officer will monitor and, if and when necessary, report upon the effectiveness of these arrangements.

Annex 3 - Investment management practices for non treasury investments

The Council recognises that investment in other financial assets and property primarily for financial return, taken for non-treasury management purposes, requires careful investment management. Such activity includes loans supporting service outcomes, investments in subsidiaries and investment property portfolios. The Council will ensure that all of its investments are covered in its annual Capital Strategy, and will set out, where relevant, the Council's risk appetite and specific policies and arrangements for non-treasury investments. It will be recognised that the risk appetite for these activities may differ from that for treasury management. The Council will maintain a schedule setting out a summary of existing material investments, subsidiaries, joint ventures and liabilities including financial guarantees and the Council's risk exposure.