AUDIT, GOVERNANCE & STANDARDS COMMITTEE	15 January 2018

Treasury Management Strategy 2018/19

Final Decision-Maker	Council
Lead Head of Service/Lead Director	Mark Green, Director of Finance & Business Improvement
Lead Officer and Report Author	John Owen – Finance Manager
Classification	Public
Wards affected	None

Executive Summary

This report sets out the draft Treasury Management Strategy for 2018/19 for consideration by the Audit, Governance & Standards Committee and recommendation to Council for adoption. The strategy statement and associated documents are attached as Appendices A-C to this report.

This report makes the following recommendations to this Committee:

1. That the Treasury Management Strategy for 2018/19 attached at Appendix A to this report is agreed and recommended to Council for adoption, subject to any amendments arising from consideration of the Capital Programme by Policy and Resources Committee at its meeting on 24th January 2018.

Timetable	
Meeting	***Date***
Audit, Governance & Standards Committee	15th January 2018
Council	28th February 2018

Treasury Management Strategy 2018/19

1. INTRODUCTION AND BACKGROUND

1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year must meet cash expenditure. The Treasury Management Strategy assists the Council in achieving this objective while maintaining value for money.

1.2 The first function of the Council's 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.

1.3 The second main function of the treasury management operation is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council, so this means 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. On occasion any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.4 The council has adopted the Treasury Management in Public Services: Code of Practice 2011 Edition ('the Code') issued by the Chartered Institute of Public Finance and Accountancy (CIPFA). 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."*

1.5 The current 2017/18 Strategy was reviewed by this Committee and agreed by Council in March 2017. A mid-year monitoring report was considered by this Committee at its November meeting. Essentially the Council are taking a similar stance with its Strategy for 2018/19, which is:

- to utilise cash balances rather than loan debt to finance the capital programme in the short term, due to low investment returns and high counterparty risk in the current economic climate;

- to further diversify its portfolio, as far as is operationally feasible, ensuring that a combination of secured and unsecured investments are considered. Greater use of Local Authority investments will be sought due to the high security of the borrower which enables investment over a longer period where funds are not required immediately.

1.6 The strategy statement is set out at **Appendix A** to this report. It is consistent with the requirements of the CIPFA and DCLG and has been developed in line with currently approved spending and financing proposals.

1.7 **Appendix B** details the proposed list of investment counterparties based on current ratings against the selection criteria set out in the strategy.

1.8 The Policy & Resources Committee will consider a capital programme for the period 2018/19 to 2022/23 at its meeting on 24th January 2018. The attached Strategy includes assumptions about the Capital Programme and it is not anticipated that the Capital Programme as finally agreed will differ significantly from these.

1.9 This strategy is compiled in accordance with the current Treasury Management Code of Practice. The Government has recently consulted on proposed changes to the Prudential Framework. The Government's proposed changes, as circulated for consultation, are not so restrictive as to prevent the relatively limited use of prudential borrowing anticipated by the Council. However, if the changes finally implemented to the Prudential Framework require the Treasury Management Strategy to be amended, an updated strategy will be presented to the Audit, Governance & Standards Committee for scrutiny during 2018.

1.10 The following table shows the maximum and expected prudential borrowing required to fund the draft capital programme. The maximum borrowing limit excludes any internal borrowing:

	2018/19 £	**2019/20 £**	**2020/21 £**
Capital Programme	23,947,645	22,635,500	15,303,330
Other Funding Streams (incl. New Homes Bonus)	(4,000,000)	(4,200,000)	(800,000)
Maximum Prudential Borrowing	19,947,645	18,435,500	14,503,330
Estimated Internal Borrowing	(18,401,000)	0	0
Expected Borrowing	1,546,645	18,435,500	14,503,330

1.11 The prudential indicators for the proposed strategy are set out within **Appendix C** to this report.

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2. AVAILABLE OPTIONS

2.1 **Option 1:** The Committee could decide not to recommend the strategy to Council. The Council must adopt a strategy for 2018/19 and should the Committee decide not to recommend the attached strategy it would need to recommend an alternative to Council. The strategy is in line with the necessary codes and practice guides and takes a low risk approach favouring liquidity over return and as such is considered suitable for this Council.

2.2 **Option 2:** Subject to any legal obligations placed upon the Council, the Committee could amend the strategy prior to recommendation to Council. The Committee would need to provide Council with detailed reasons for the amendment and the risks and benefits that the proposed amendment provides in order for the Council to make a fully informed decision on the recommendation. Areas where amendments could be made include the following, which are detailed along with current reasons for not changing

2.2.1 Limits: the proposed strategy allows maximum investments with certain institutions of £8m. The current limit could be retained, increased or reduced. Given the difficulty in identifying opportunities to lend at suitable rates within the counterparty list, it is considered appropriate to incorporate sufficient flexibility by retaining the current limit for investments with the most secure organisations.

2.2.2 Counterparties: the proposed strategy allows non-specified investments with other local authorities and the rated/unrated building societies that are within Arlingclose's suggested counterparty list. The strategy could propose to utilise additional counterparties from the non-specified investments group. However, due to the fact that this would involve an increased level of risk to the security of the council's cash, this is not considered to represent a prudent course of action.

2.2.3 Alternative use of cash: the resources invested in expenditure could be utilised to deliver key priority outcomes. However the core cash held by the Council is either set aside for future expenditure, such as the capital programme, or held as a form of risk mitigation, such as the minimum level of revenue balances. To utilise these resources for alternative projects could compromise liquidity and put the Council at future risk should an unforeseen event occur.

2.2.4 External Fund Managers: by appointing external managers local authorities may possibly benefit from security of investments, diversification of investment instruments, liquidity management and the potential of enhanced returns. Managers do operate within the parameters set by local authorities but this involves varying degrees of risk. This option has been discounted on the basis of the risk which would make it difficult to ascertain a suitable sum to assign to an external manager.

2.3 **Option 3:** The Committee could agree the attached strategy and recommend it to Council. The attached strategy has been produced in line with current guidance from CIPFA and the Department for Communities and Local Government (DCLG) and has been reviewed by the Council's Treasury Management Advisors and their recommended amendments have been taken into account.

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3. PREFERRED OPTION AND REASONS FOR RECOMMENDATIONS

3.1 The recommended option is Option 3, to recommend to Council the strategy set out in Appendix A. In agreeing this option the committee should note the potential change in the level of prudential borrowing if there are any changes to the council's proposed capital spending plans.

3.2 As stated above, the proposed strategy has been produced in line with current guidance from CIPFA and the Department for Communities and Local Government (DCLG).

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4. RISKS

4.1 Detailed risk management policies are included within the Treasury Management Practices to which the Council adheres to. A brief description of these risks along with the Council's actions to mitigate these risks are as follows:

Liquidity Risk - Liquidity risk is the risk that cash not be available when it is required. The Council has sufficient standby facilities to ensure that there is always sufficient liquidity to deal with unexpected occurrences. The Council also has an overdraft facility with Lloyds Bank of £500,000 plus the option of short term borrowing.

Interest Rate Risk - Interest rate risk is the risk that unexpected changes in interest rates expose the Council to greater costs or a shortfall in income than have been budgeted for. The Council will seek to minimise this risk by seeking expert advice on forecasts of interest rates from treasury management consultants and agreeing with them its strategy for the coming year for the investment and debt portfolios. It will also determine appropriate limits and trigger points which are set out in the annual Treasury Management Strategy Statement .

Exchange Rate Risk - Exchange rate risk is the risk that unexpected changes in exchange rates expose the Council to greater costs or a shortfall in income than have been budgeted for. The Council has a minimal exposure to exchange rate risk as it has no powers to enter into loans or investments in foreign currency for treasury management purposes.

Inflation Risk - Inflation risk is the risk that unexpected changes in inflation expose the Council to greater costs or a shortfall in income than have been budgeted for. Inflation both current and projected will form part of the debt and investment decision-making criteria both within the strategy and operational considerations

Credit and Counterparty Risk - Credit and counter-party risk is the risk of failure by a third party to meet its contractual obligations under an investment, loan or other commitment, especially one due to deterioration in its creditworthiness, which causes the Council an unexpected burden on its capital or revenue resources. Treasury management staff will add or delete counterparties to/from the approved counterparty list in line with the policy on criteria for selection of counterparties. Due to volatility of the financial market, Treasury Management staff will use information from various sources, eg brokers, Treasury Management Consultants and other local Authority experience to determine the credit worthiness of an institution and to decide if funds are at risk and agree best course of action with Director of Finance & Business Improvement.

Refinancing Risk - Refinancing risk is the risk that when loans or other forms of capital financing mature, that they cannot be refinanced where necessary on terms that reflect the assumptions made in formulating revenue and capital budgets. The Council is currently debt-free, however it will soon be looking to borrow to fund its capital programme in the coming years. In considering the affordability of its capital plans, the Council will consider all the resources currently available/estimated for the future together with the totality of its capital plans, revenue income and revenue expenditure forecasts for the forthcoming year and the two following years and the impact these will have on council tax. It will also take into account affordability in the longer term beyond this three year period.

Legal and Regulatory Risk - Legal and regulatory risk is the risk that either the Council, or a third party which it is dealing with in its treasury management activities, acts outside of its legal powers or regulatory requirements and as a result the Council incurs loss. The treasury management activities of the Council shall comply fully with legal statute, guidance, Codes of Practice and the regulations of the Council. The Authority will provide written evidence of its powers and authorities to any counterparty that requests us to do so. Counterparties will also provide their details to the Authority as a matter of course.

Fraud, Error and Corruption Risk - Fraud, error and corruption risk is the risk that the Council may fail to employ adequate systems, procedures and other arrangements which identify and prevent losses through such occurrences. The Council will seek to ensure an adequate division of responsibilities and maintenance at all times of an adequate level of internal checks which minimises such risks along with maintaining records of all treasury management transactions so that there is a full audit trail and evidence of the appropriate checks being carried out. Delegated members of staff have the responsibility for the treasury management function for the Council and the Director of Finance & Business Improvement authorises who these are. The Council also has a Fidelity Guarantee insurance policy with Zurich Insurance which covers against loss of cash through fraud or dishonesty of employees.

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5. CONSULTATION RESULTS AND PREVIOUS COMMITTEE FEEDBACK

5.1 None.

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6. NEXT STEPS: COMMUNICATION AND IMPLEMENTATION OF THE DECISION

6.1 This report will be considered by Council at its meeting on 28th February 2018.

7. CROSS-CUTTING ISSUES AND IMPLICATIONS

Issue	Implications	Sign-off
Impact on Corporate Priorities	We do not expect the recommendations will by themselves materially affect achievement of corporate priorities. However, they will support the Council's overall achievement of its aims as set out in section 3.	Head of Finance
Risk Management	Already covered in the risk section of the report.	Head of Finance
Financial	This report relates to the financial activities of the Council in respect of treasury management and specific financial implications are therefore detailed within the body of the report.	Director of Finance & Business Improvement
Staffing	None	
Legal	The report is in compliance with statutory and legal regulations, e.g. CIPFA Code of Practice on Treasury management in local authorities.	Legal Team
Privacy and Data Protection	None	
Equalities	None	
Crime and Disorder	None	
Procurement	None	

8. REPORT APPENDICES

The following documents are to be published with this report and form part of the report:

- Appendix A: Treasury Management Strategy Statement
- Appendix B: Proposed List of Investment Counterparties
- Appendix C: Prudential Indicators

9. BACKGROUND PAPERS

9.1 None