

The Treasury Management Strategy, Prudential Indicators 2010/11 and Annual Investment Strategy 2010/11 and Performance for 2009/10

Audit Committee

Date: 22nd June 2010

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Parish / Wards Affected: All

Purpose

- The revised Treasury Code of Practice recommended that each council must delegate the role of scrutiny of treasury management strategy and policies to a specific named body. Cabinet approved in February 2010 that Audit Committee should act as this body.
- To report changes to the CIPFA Treasury Management Code of Practice
- To report the Treasury Management Strategy and Annual Investment Strategy for the Council for 2010 -11 and Prudential Indicators for the period 2010/11 - 2012/13
- To report the Minimum Revenue Provision (MRP) Policy for 2010/11
- To report Treasury Management Performance for 2009/10

1. INTRODUCTION

The Revised CIPFA Treasury Management Code of Practice 2009

- 1.1. Treasury management is concerned with how organisations manage their cash resources and its scope covers borrowing and investment strategies and techniques. Risk is inherent in all treasury management activities and it is necessary to balance risk and return across the overall portfolio. However, the general overriding priority is to protect capital rather than maximise return.
- 1.2. In the light of the Icelandic banking situation in 2008, CIPFA has amended the CIPFA Treasury Management in the Public Services Code of Practice (the Code) and the template for the revised Treasury Management Policy Statement.
- 1.3. It is a requirement of the Code for it to be formally adopted, and the revised Code is therefore attached at appendix 1. The revised Treasury Management Policy Statement attached at Appendix 2 should also be noted.
- 1.4. The revised Code has emphasised a number of key areas:
 - All councils must formally adopt the revised Code and four clauses;

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- The strategy report will affirm that the effective management and control of risk are prime objectives of the Council's treasury management activities;
- The Council's appetite for risk must be clearly identified within the strategy report and will affirm that in general priority is given to security of capital and liquidity when investing funds and explain how that will be carried out;
- Responsibility for risk management and control lies within the organisation and cannot be delegated to any outside organization;
- Credit ratings should only be used as a starting point when considering risk. Use should also be made of market data and information, the quality financial press, information on government support for banks and the credit ratings of that government support;
- Councils need a sound diversification policy with high credit quality counterparties and should consider setting country, sector and group limits;
- Borrowing in advance of need is only to be permissible when there is a clear business case for doing so and only for the current capital programme or to finance future debt maturities;
- The main annual treasury management reports MUST be approved by full Council;
- There needs to be, at a minimum, a mid year review of treasury management strategy and performance. This is intended to highlight any areas of concern that have arisen since the original strategy was approved;
- Each council must delegate the role of scrutiny of treasury management strategy and policies to a specific named body;
- Treasury management performance and policy setting should be subjected to prior scrutiny;
- Members should be provided with access to relevant training;
- Those charged with governance are also personally responsible for ensuring they have the necessary skills and training;
- Responsibility for these activities must be clearly defined within the organisation, with a suggested model scheme of delegation set out at Appendix 3 and the Role of the S.151 Officer as set out at Appendix 4
- Officers involved in treasury management must be explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Council (this will form part of the updated Treasury Management Practices).

1.5. This strategy statement has been prepared in accordance with the revised Code. Accordingly, the Council's Treasury Management

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Strategy will be approved annually by the full Council and there will also be a mid year report. In addition there will be monitoring reports and regular review by board members in both executive and scrutiny functions. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the treasury management function appreciate fully the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

- 1.6. This Council will adopt the reporting arrangements in accordance with the requirements of the revised Code as detailed at Appendix 5.

Revised CIPFA Prudential Code

- 1.7. CIPFA also issued a revised Prudential Code in November 2009, which primarily covers borrowing and the Prudential Indicators. The key changes were an increased emphasis on asset management and capital programming. In addition, some treasury management indicators were removed and transferred to the Treasury Management Code.

2. TREASURY MANAGEMENT STRATEGY FOR 2010/11

- 2.1. The Local Government Act 2003 (the Act) and supporting regulations requires the Council to 'have regard to' the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable.
- 2.2. The Act therefore requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy, which sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.
- 2.3. The suggested strategy for 2010/11 in respect of the following aspects of the treasury management function is based upon the treasury officers' views on interest rates, supplemented with market forecasts provided by the Council's treasury adviser, Sector Treasury Services. The strategy covers:
- treasury limits in force which will limit the treasury risk and activities of the Council;
 - Prudential and Treasury Indicators;

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- the current treasury position;
- the borrowing requirement;
- prospects for interest rates;
- the borrowing strategy;
- policy on borrowing in advance of need;
- debt rescheduling;
- annual Minimum Revenue Provision Report (MRP) and Policy Statement.

2.4. The full strategy for 2010/11 is set out at Appendix 6 and Prudential Indicators at Appendix 7.

3. ANNUAL INVESTMENT STRATEGY

3.1. The 2004 investment guidance requires that authorities in England and Wales produce an annual investment strategy (AIS), approved and, if necessary, amended by the full Council, to be made publicly available. It should set out the policies for managing investments and for giving priority to the security and liquidity of those investments.

3.2. In particular, the annual investment strategy includes:

- policies on the use of credit ratings and credit ratings agencies;
- procedures for determining and limiting the use of higher risk investments, and for the liquidity of investments;
- information around the of an external treasury management external;
- the schemes of delegation and the role of the S151 officer.

3.3. The proposed annual investment strategy is attached at Appendix 8.

3.4. The Council has a requirement to provide an annual policy around the Minimum Revenue Provision. This relates to Capital expenditure which is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, machinery etc. It would be impractical to charge the entirety of such expenditure to revenue in the year in which it was incurred, therefore such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision. The statement is contained at Appendix 9.

4. TREASURY MANAGEMENT PERFORMANCE 2009/10

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4.1. The Council is involved in two types of treasury activity, both of which are affected by the economic environment:

- Borrowing for capital purposes and for temporary cash flow purposes
- Investment of surplus cash

4.2. The strategy and performance in respect of each of these two activities is summarised in the sections below.

Borrowing

4.2.1. Two new long-term loans were taken out in November 2009, both with Royal Bank of Scotland, for £20m and £10m. These are “stepped” rate loans where the Council will pay a low initial rate for 3 years linked to the London Inter Bank Offer Rate followed by a fixed rate after 3 years. In 2009/10 the average rate paid on these loans was 0.62%, and after 3 years these loans will revert to a fixed rate of 4.35% and 4.2% respectively. By structuring its new debt in this year the Council has attempted to match the borrowing rate with the achievable investment rates in order to minimise any cost of carry for 3 years. During the year, the Council also repaid a £12.35m loan (2.07%) as well of £76k of minor Annuity and Equal Instalments of Principal (EIP) loans.

4.2.2. The average rate the Council paid on all debt (both long term and short term) in 2009/10 was £4.36%. This is a reduction of 0.57% from the previous financial year. The Councils total long term debt has increased by £17.6m to £103.5m as at 31 March 2010.

4.2.3. Although the Council has a significant long-term borrowing requirement, the strategy was to fund a significant proportion of capital expenditure from reducing its investments rather than undertaking more expensive new borrowing. This is because the rates achievable on the Councils investments are lower than the rates that would be payable on long term borrowing. The Council funded approximately £28m of its Capital expenditure in this way. However, this will not be possible at the same levels in 2010/11 as investment balances are now much lower than in 2009/10.

Lending

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4.2.4. The Council's agreed Treasury Policy states that The Council utilises the creditworthiness service provided by Sector Treasury Services. This service uses credit ratings from the three main ratings agencies as well as overlaying other relevant market data. Sector then recommends a duration that counterparties should be invested with of between 3 months and 2 years.

4.2.5. The Council utilises these recommendations in making its investment decisions but in order to further ensure the security of taxpayers funds, will only lend to counterparties which sector recommends as being in the 6 month band and will not lend to any counterparty for more than 1 year.

4.2.6. In common with most local authorities, Swindon Borough Council manages a large proportion of its investment portfolio in-house, but also employs an external fund manager, Investec, who held £36.8 million of the Council's total short-term investments at the end of the financial year. The main reason for adopting this approach is due to the fund manager's particular expertise in the bond market and other very specialist treasury instruments which, in certain market conditions, can yield better rates of return than standard cash investments and allows the Council to maintain a more diverse investment portfolio that it could maintain in house. The rate of return for the Council's external fund manager for 2009/10 was 1.3% net of management fees. This figure is set against an agreed benchmark '7 day' rate of 0.38%.

4.2.7. During 2009/10 an average daily balance of £45.1m million was being managed in-house. This balance was sufficient to manage the peaks and troughs of the Council's cash flows and provide the flexibility to choose longer investment periods and take advantage of higher interest rates available. In total, interest of £634k was earned in 2009/10 on these investments at an average rate of 1.39%. Over the full year, this rate exceeded the "benchmark" 7-day rate of 0.38%.

5. The Council's debt and investment position as at 31 March 2010 is shown in the table below:

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Analysis of Debt and Investments

| Debt & Investments | 31/03/2009 | | 31/03/2010 | | Difference | |
|--------------------------------|---------------|--------------|----------------|--------------|-----------------|---------------|
| | £'000 | Rate (%) | £'000 | Rate (%) | £'000 | Rate (%) |
| Long Term Debt PWLB | 85,500 | 4.93% | 73,049 | 5.19% | (12,451) | 0.26% |
| Long Term Debt Market | 0 | 0 | 30,000 | 0.62% | 30,000 | 0.62% |
| Total Long Term Debt | 85,500 | 4.93% | 103,049 | 4.65% | 17,549 | -0.28% |
| In House Investments | 34,500 | 5.80% | 36,845 | 1.39% | 2,345 | -4.41% |
| Externally Managed Investments | 24,500 | 5.76% | 35,000 | 1.30% | 10,500 | -4.46% |
| Total Investments | 59,000 | 5.78% | 71,845 | 1.36% | 12,845 | -4.42% |
| Short-term Borrowing | (700) | | (30,350) | | | |
| Net Investment Position | 58,300 | | 41,495 | | (16,805) | |

Note: PWLB – Public Works Loan Board

Compliance with Treasury Limits

6. During the 2009/10 Financial Year all Treasury activity was carried out within the Council's Treasury limits and Prudential Indicators as set out in the Council's Treasury Policy Statement and annual Treasury Strategy Statement. The actual Prudential Indicators for 2009/10 can be found in Appendix 7.

Alternative Options

No alternative options are proposed. The Cabinet could decide not to support the recommendations.

Risk Management

Financial and Procurement Implications

The Prudential Code requires the following matters to be taken into account when setting or revising prudential indicators:-

- (a) Option appraisals for all capital projects (to demonstrate value for money)
- (b) Asset management (to demonstrate stewardship of the Councils assets)
- (c) Strategic planning for the authority (to demonstrate service objectives prioritisation).

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- (d) Achievability of the forward plan (to demonstrate the realism of the plan)
- (e) Implication for external borrowing (i.e. prudence)
- (f) Implication for Council Tax and housing rents (i.e. affordability)

Items (a)-(c) are largely considered in the current arrangements as part of the asset management planning/corporate capital strategy processes; items (d) and (f) - in financial terms - are dealt with as part of the Medium Term Financial Planning and Budget setting processes; and item (e) is inherent to the prudential indicator setting process itself.

Legal/Human Rights Implications

- Legal and Human Rights implications have been considered in the preparation of this report.

Links to Corporate Plans and Policies (in particular to Swindon 2010 Promises)

- The effective management of cash resources through robust treasury management processes underpins the Council's ability to achieve its plans and priorities.

Consultees

The Director of Finance and the Director of Law and Democratic Services are consulted on all reports.

Appendices

- Appendix 1 - Adoption of the revised CIPFA Treasury Management Code of Practice 2009
- Appendix 2 - Treasury Management Policy Statement
- Appendix 3 - Treasury management scheme of delegation
- Appendix 4 - The treasury management role of the section 151 officer
- Appendix 5 – Reporting requirements
- Appendix 6 - The Treasury Management Strategy
- Appendix 7 - The Prudential Indicators for Capital, External Debt and Treasury Management 2009/10 – 2011/12 and further information
- Appendix 8 - Annual Investment Strategy
- Appendix 9 - Annual Minimum Revenue Provision Report

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Background Papers and Appendices

- Draft Budget report to Cabinet 10 February 2010
- Consultation responses and notes of consultation meetings and forums

Key Decision in Forward Plan

This is not a key decision for Cabinet as Council will make the decision on 22 February 2010 and this decision is in the Cabinet's Forward Plan for February 2010