Mid-Year Treasury Performance 2016-17

Cabinet **Date: 7 December 2016**

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Wards:	All
Locality Affected:	All
Parishes Affected:	All

1. Purpose and Reasons

1.1 This report sets out the mid-year Treasury Management performance for 2016/17 and proposals for amendments to the Councils Minimum Revenue Policy.

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

2. Recommendations

Cabinet is recommended to:

2.1 Note the mid-year Treasury Management performance;

2.2 Recommend the amendment to the Minimum Revenue Provision Policy, as set out in Appendix 1, for approval by Full Council on 26 January 2017

3. Detail

3.1 The CIPFA Treasury Code of Practice recommends that Treasury Management performance is reported at least twice a year. This report sets out the mid-year performance for the Council to the end of September 2016.

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

3.2.1 Borrowing long-term for capital investment purposes, and short-term for temporary cash flow purposes;

3.2.2 Investment of surplus cash.

3.3 The performance in respect of each of these two activities is summarised below.

Borrowing

3.4 There has been no new long term borrowing (loans with a maturity of greater than a year) in the first 6 months of this financial year.

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3.5 In addition to long-term borrowing, the Council also undertakes short-term borrowing in order to smooth out peaks and troughs in its daily cash flow. As at the 30th September 2016, the Council had £12m of short-term borrowing running at an average rate of 0.39%. It should be emphasised that as short-term borrowing is undertaken in respect of daily cash flow activities, this figure can fluctuate significantly from day to day dependent on income received or payments due out.

3.6 The Council's total long-term debt decreased from £285.8m on 31st March 2016 to £285.0m as at 30th September 2016 as a small element of loans matured and were not replaced. The overall long-term borrowing rate remains at 3.53%.

3.7 The Council's average rate on all debt (both long term and short term) for the year to 30th September 2016 is 3.41%, which is a slight increase from 3.39% at the end of the previous financial year.

3.8 There is a significant long-term borrowing requirement to fund the underlying capital programme and loans will be taken out as and when officers deem rates to be advantageous. It is currently still financially advantageous for the Council to fund capital expenditure from using internal cash balances as opposed to new external loans.

Investments - Lending

3.9 As at the 30th September 2016, investments stood at £77.2m running at an average rate of 1.48%.

3.10 There are three main categories of investment:

3.10.1 Liquid Investments – investments that are instantly accessible and are used primarily to smooth the peaks and troughs in the Council's daily cash flow. These include money market funds, instant access accounts and any balances in our own bank account. The average balance on these funds was £19m over the first 6 months of the year achieving an average investment rate of 0.40%.

3.10.2 Fixed Term investments – these are locked in for a specific period of time and therefore gain the maximum return (once security and liquidity have been ensured using the Council's creditworthiness parameters.) These investments are made with banks for a fixed term up to 2 years. The average balance of these investments over the first 6 months was £43.2m, achieving an average rate of 0.90% comparing favourably with the benchmark 3 Month LIBOR rate of 0.51%.

3.10.3 Local Authority Property Fund ("LAPF") - £15m is invested in this fund and the average rate of return on this investment so far is 4.54 %.

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3.10.4 The LAPF gives local authorities an exposure to a diversified portfolio of commercial property throughout the UK and its objectives are to generate long-term growth in capital and an attractive income over time (5 years or more). The trustees of the fund are the Local Authorities' Mutual Investment Trust (LAMIT) a body controlled by representatives of the Local Government Association, the Convention of Scottish Local Authorities, the Northern Ireland Local Government Officers' Superannuation Committee and investors in the Fund.

3.11 The standard comparator for investment performance for portfolios similar to ours is the 3 Month LIBOR rate, which for the year to 30th September 2016 stood at 0.51%. The Council exceeded this rate with an average return on its investments over the 6 month period of 0.75% on an average investment balance of £62.2m. (Excluding the property fund)

3.12 The Council's debt and investment position as at 30th September 2016 compared with 31st March 2016 is shown in the table below:

Analysis of Debt and Investments

Debt & Investments	**31/03/2016**		**30/09/2016**	
	£'000	**Rate (%)**	**£'000**	**Rate (%)**
Long Term Debt PWLB	240,757	3.54%	240,007	3.54%
Long Term Debt Market	45,000	3.43%	45,000	3.43%
Total Long Term Debt	**285,757**	**3.53%**	**285,007**	**3.53%**
Short-term Borrowing	7,680	0.46%	12,000	0.39%
Total Debt	**293,437**	**3.39%**	**297,007**	**3.41%**
Investments	(59,000)	1.36%	(77,200)	1.48%
Net Borrowing Position	**234,437**		**219,807**	

Compliance with Treasury Limits

3.13 During the 2016/17 Financial Year to date, all Treasury activity has been carried out within the Council's Treasury limits and Prudential Indicators, as set out in the Council's Treasury Management Strategy.

Proposed Changes to Minimum Revenue Policy

3.14 Minimum Revenue Provision (MRP) is statutory requirement to make a charge to the Council's General Fund to make provision for the repayment of the Council's borrowing liabilities (past capital debt and other credit liabilities such as PFI)

3.15 The scheme of MRP was set out in former regulations 27, 28 and 29 of the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 ("The 2003 Regulations"). This system was radically revised in 2008 by the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008, which shifted the emphasis from regulations to guidance. The new system and accompanying guidance replaced the prescriptive MRP calculation with a statutory duty "to determine for the current financial year an amount of MRP which it considers to be prudent" and in doing so to "have regard" to the guidance and recommendations within it. The key principle is that an authority's debt liability should be repaid over a similar period to that which the asset associated with the capital expenditure provides benefits or, in the case of borrowing supported by Revenue Support Grant , in-line with the period implicit in the determination of that grant (i.e. 4% p.a.). The guidance sets out four options that are consistent with this principle. Local authorities are asked by the Secretary of State "to prepare an annual statement of their policy on making MRP for submission to their full Council".

3.16 The type of approach intended by the MRP guidance is clearly to enable local circumstances and discretion to play a part, as the guidance in general contains a set of recommendations rather than representing a prescriptive process. The guidance makes it clear that councils can follow an alternative approach, provided they still make a prudent provision.

3.17 Officers have reviewed the Council's current approach in consultation with the Council's Treasury Management Advisors, Capita Asset Services, and make the following recommendations:-

The annuity method for unsupported borrowing

3.18 For all unsupported borrowing, a change from the 'straight line method' to the 'annuity method' - one of the options set out in the Guidance – is recommended in place of the straight-line charge currently applied across the asset life.

3.19 The annuity method results in a back loaded charge and results in savings in earlier years, with higher costs in later years. It makes provision for an annual charge to the General Fund which, unlike the current Straight Line method, takes account of the time value of money (whereby paying £100 in 10 years' time is less of a burden than paying £100 now). The schedule of charges produced by the annuity method thus results in a consistent charge over an asset's life, taking into account the real value of the annual charges when they fall due.

3.20 It is proposed that the annuity method is applied to all unsupported borrowing incurred going forwards and from 2016/17 onwards, over the remaining life, for unsupported borrowing expenditure incurred prior to 2016/17.

3.21 It is also proposed that the annuity method is applied retrospectively for all unsupported borrowing incurred since April 2008 when the 2008 regulations and guidance were brought in.

PFI – annuity method over asset life

3.22 The Annual Unitary Charge ("U/C") payment for the Council's schools PFI is split into a services element and a finance lease element (representing the debt finance for the buildings). The Council charges MRP on the asset (in line with how it would treat any capital expenditure financed from borrowing) and this is currently provided at the amount equivalent to the finance element of the U/C. The U/C is funded fully through schools/council contributions and government grant so currently there is no real revenue impact of charging MRP in this way.

3.23 MRP on the Council's PFI project is currently provided for on the basis of the contract life through to 2032. This is inconsistent with how the Council provides for MRP on other buildings financed from borrowing as MRP is currently provided for these assets on the basis of their expected asset life, typically 50 years. The PFI contract specifies that the buildings were designed with a 60 year asset life to 2065, an additional 33 years beyond the existing contract expiry date.

3.24 It is proposed that from 2016/17 MRP relating to PFI schemes is charged by using the annuity method over the remaining useful economic lives of assets. This would mean that MRP better matches the life of the assets associated with the debt liability arising from the contract, in accordance with the main principles of the MRP guidance, and is consistent with the Council's proposed treatment for all other unsupported capital expenditure.

Use of capital receipts to fund PFI liability repayment

3.25 Regulation 23 of the 2003 Regulations, introduced via Statutory Instrument 2003 No. 3146, provides that capital receipts can be used "to meet any liability in respect of credit arrangements, other than any liability which, in accordance with proper practices, must be charged to a revenue account".

3.26 The finance repayment element of the U/C is a "liability in respect of a credit arrangement" and therefore could be funded through using capital receipts rather than revenue funding. At the time of writing, £600k of non-ring-fenced capital receipts had been identified, which could be used to repay the debt liability in lieu of an equivalent amount of MRP, which would release an equivalent amount of revenue funding.

<u>Financial Implications of change to MRP policy</u>

3.27 The impact of the proposed changes to the MRP policy, if all changes were made, is shown in the table below. These are indicative and will be finalised as

part of the 2016/17 Statement of Accounts process, which is also subject to external audit. Consideration will also be given as to how these savings will be taken into account with the budget position.

Policy change	Indicative Saving 2016/17 (£'000)	Indicative saving 2017/18 (£'000)	Indicative saving 2018/19 (£'000)	Indicative saving 2019/20 (£'000)	Indicative saving 2020/21 (£'000)
Change to Annuity method for unsupported borrowing from 2016/17	2,652	2,568	2,485	2,406	2,323
Annuity method for unsupported borrowing backdated to 2008	1,538	2,196	2,164	2,084	2,025
Annuity method for PFI MRP on asset life basis	565	700	856	1,032	1,230
Sub-total annual recurring savings	**4,755**	**5,464**	**5,505**	**5,522**	**5,578**
One off - use of estimated capital receipts to fund PFI repayment	800est	800est	n/k	n/k	n/k
Total potential recurring and one-off	**5,555**	**6,264**	**5,505**	**5,522**	**5,578**

3.28 Appendix 1 details the current MRP policy as well as the proposed revised policy

4. Alternative Options

4.1 Any alternative options for specific areas are set out within the report.

5. Implications, Diversity Impact Assessment and Risk Management

Financial and Procurement Implications

5.1 These have been reflected in the body of the report.

Legal and Human Rights Implications

5.2 All legal and human rights considerations have been taken fully into account in compiling this report. It is considered that the recommendations of this report are compatible with Convention rights.

All Other Implications (including Staff, Sustainability, Health, Rural, Crime and Disorder)

5.3 There are no such direct implications.

Diversity Impact Assessment (DIA)

5.4 There is no impact on DIA associated with management of the Councils cash balances.

Risk Management

5.5 There are no direct risks arising from this report.

6. Consultees

6.1 The Interim Corporate Director, Resources (Section 151 Officer) and Director of Law and Democratic Services (Monitoring Officer) are consulted in respect of all reports.

7. Background Papers

7.1 None.

8. Appendices

8.1 Appendix 1 – Proposed Revised minimum Revenue Provision Policy.

9. Key Decision/Decision in Cabinet Work Programme and Forward Plan

9.1 This is not a key decision and is included in the Cabinet Work Programme and Forward Plan for September 2016.

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