CAB1377
FOR DECISION
WARD(S): GENERAL

CABINET

13 February 2007

TREASURY MANAGEMENT

REPORT OF THE DIRECTOR OF FINANCE

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RECENT REFERENCES:

CAB1174 Treasury Management 7 February 2006

CAB1308 Treasury Management Stewardship Report 13 September 2006

EXECUTIVE SUMMARY:

This report covers the Policy Statement and Treasury Management Strategy for 2007/08 considers them in the light of the Prudential Code published by CIPFA and the CLG Investment Guidelines and recommends them for adoption by the Council.

RECOMMENDATIONS:

1. That Cabinet recommends to Council that the Treasury Management Strategy for 2007/08, including the prudential indicators contained therein, as detailed in Appendix B, be approved.

CABINET

13 February 2007

TREASURY MANAGEMENT

REPORT OF THE DIRECTOR OF FINANCE

1 Introduction

1.1 The regulatory framework for capital finance and investment in local government is covered by a system based largely on self regulation. This system requires local authorities to make sure their capital spending plans are affordable, prudent and sustainable.

1.2 Key aspects of the system are the *Code of Practice for Treasury Management in the Public Service*s and the *Prudential Code for Capital Finance in Local Government*, both developed by the Chartered Institute of Public Finance and Accountancy (CIPFA), and the *Guidance on Local Government Investments* drawn up by the Department for Communities and Local Government (CLG).

1.3 The City Council complies with these codes and the investment guidance.

2 Prudential Code

2.1 Local authorities determine their own programmes for capital investment in fixed assets that are central to the delivery of quality public services. The Prudential Code has been developed as a professional code of practice to support local authorities in taking their decisions. They 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.

2.2 The key objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable. A further key objective is to ensure that treasury management decisions are taken in accordance with good professional practice and in a manner that supports prudence, affordability and sustainability.

2.3 To demonstrate that local authorities have fulfilled these objectives, the Prudential Code sets out indicators that must be used and factors that must be taken into account. These indicators are designed to support and record local decision making in a manner that is publicly accountable.

2.4 The Prudential Code includes the following as required indicators in respect of treasury management:

a) Compliance with the CIPFA *Code of Practice for Treasury Management in the Public Services.*

b) Upper limits on fixed interest rate and variable interest rate exposures.

c) Upper and lower limits for the maturity structure of borrowings.

d) Authorised borrowing limits, including other long term liabilities.

e) The minimum amount to be held in short term investments.

f) Upper limit for principal sums invested for periods longer than 364 days.

2.5 Further commentary on these indicators is given below.

2.6 (b) *The upper limits on fixed interest rate and variable interest rate exposures are set at 100% for fixed rate and 20% for variable rate exposure.* This applies to both borrowing and investments. It is not anticipated that the authority would either borrow or invest at variable interest rates but this option is retained in case a suitable opportunity arises.

2.7 (c) *The upper limit for borrowing is set at 100% for under 12 months, 100% for between 12 and 59 months and 100% for 5 years and above – the lower limit is set at 0% for periods up to 5 years and 0% for periods of 5 years and above.* The periods are defined within the Code and setting the limits at 100% for all periods provides maximum scope for borrowing lest the Council be in a position to borrow in future. In practice, it is unlikely that any borrowing other than for short term cash flow purposes will be undertaken in the coming year.

2.8 (d) *The authorised limit for borrowing is set at £7 million, including £2 million for other long term liabilities with an operational boundary of £2 million.* The authorised limits on borrowing are required to be set but the operational boundary is the likely scenario. As the authority is debt free, it is unlikely that the Council will need to borrow more than £2m for periods of a few weeks to overcome temporary cashflow shortages. However, as with the other indicators, flexibility is built in so that, should the need arise, borrowing can be undertaken. The authorised limit will need to be reviewed closely in future as the project for New City Offices progresses, as it is almost certain that borrowing will be required in order to fund this development.

2.9 (e) *Upper limit for principal sums invested for periods longer than 364 days is set at £10 million.* As with other items, this limit allows flexibility for the Council. In practice, only minimal longer term investment is undertaken. It needs to be considered within the context of the next indicator – an investment of £10m would only be possible if the total investment was £50m.

2.10 (f) *The minimum amount to be held during the year in investments other than long-term investments is set at 80% of the City Council's overall investments*. Investments currently total around £30m (though historically they have been higher): at least £24m would be invested short term to meet this limit. The previous indicator also limits the amount that can be invested long term.

3 Treasury Management Policy

3.1 The City Council's Constitution contains Financial Procedure Rules in Part 4. Within those rules Section 5 refers to Borrowing and Investments. The CIPFA Code of Practice covering Treasury Management has been adopted by the City Council under Financial Procedure Rule 5.4 and the City Council applies its principles to all investment activity.

3.2 The treasury management policy statement referred to in Financial Procedure Rule 5.5 is attached as Appendix A to this report. It was first approved by the Council on 25 February 2004 and no changes are proposed for 2007/08.

4 Treasury Management Strategy for 2007/08

4.1 The Code of Practice recommends that the annual strategy should also be reported to full Council. The annual strategy report is tied in with the budget process.

4.2 The Treasury Management Strategy Report for 2007/08 is attached as Appendix B, and is recommended for approval by Cabinet and Council. Within the strategy is a statement of the proposed Treasury Management Prudential Indicators in 2007/08 for the City Council that must be approved by Council.

5 Annual Investment Strategy

5.1 One of the key requirements of the Guidance issued by CLG is that each local authority, before the start of each financial year, shall draw up an Annual Investment Strategy for the following financial year.

5.2 The strategy sets out the City Council's policies for giving priority to the security and liquidity of its investments, rather than to the yield.

5.3 The Annual Investment Strategy for 2007/08 has been incorporated in the Treasury Management Strategy for 2007/08 which is being recommended for approval by Council.

OTHER CONSIDERATIONS:

6 CORPORATE STRATEGY (RELEVANCE TO):

6.1 Treasury Management supports the Corporate Strategy by demonstrating high standards in managing the taxpayers' money.

7 RESOURCE IMPLICATIONS:

7.1 Interest rate changes continue to have a significant effect on the annual budget, generating high levels of investment income (£1.1m in the current base budget). A change of 1% alters income by £10,000 for every £1m invested, which on an investment of, say, £25m, equates to £250,000, and approximates to a council tax increase or decrease of 5%.

BACKGROUND DOCUMENTS:

Operational and financial records held in the Finance Directorate

APPENDICES:

Appendix A Treasury Management Policy Statement

Appendix B Treasury Management Strategy for 2007/08

Winchester City Council

Treasury Management Policy Statement

1 Definition of Treasury Management Activities

1.1 This Council defines its treasury management activities as:

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

2 Policy Objectives

2.1 The City Council regards the successful identification, monitoring and management of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. It also has regard to the rate of return on its investments. Accordingly, our policies and practices make clear that the effective management of risk, having regard to return, is the primary objective of our treasury management activities.

2.2 The City 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 best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management.

3 Treasury Management Practices (TMPs)

3.1 The City Council has adopted suitable treasury management practices setting out the manner in which it seeks to achieve the treasury management policies and objectives, and prescribing how it manages and controls those activities.

3.2 Treasury Management Practices are included in the Treasury Management Manual and cover:

TMP1	Risk Management
TMP2	Best value and performance management
TMP3	Decision making and analysis
TMP4	Approved instruments, methods and techniques
TMP5	Organisation, clarity and segregation of responsibilities, dealing arrangements
TMP6	Reporting requirements and management information arrangements
TMP7	Budgeting, accounting and audit arrangements
TMP8	Cash and cash flow management
TMP9	Money laundering
TMP10	Staff training and qualification
TMP11	Use of external service providers
TMP12	Corporate governance

Note The wording in 1 above differs slightly from the wording proposed by CIPFA in that the words "effective management of the risks…" are included rather than "effective control of the risks…" These words have been recommended by our brokers as controlling risk is regarded as an unachievable objective.

Winchester City Council

Treasury Management Strategy for 2007/08

1 Introduction

1.1 The Treasury Management Strategy details the current position and the expected activities of the Treasury function in the financial year 2007/08. Its production and submission to Cabinet is a requirement of the Council's approved Treasury Management Policy.

1.2 The strategy for 2007/08 is based on the anticipated movements in interest rates and the projected requirements of the City Council. The Strategy covers:

- the current portfolio position
- the investment strategy
- prospects for interest rates
- external debt
- prudential indicators

2 Current Portfolio Position

2.1 As at 31st December 2006 the Council had no external debt.

2.2 The Council had invested cash surpluses at 31st December 2006 as follows:

Non-specified Investments	
Local Authorities Mutual Investment Trust (LAMIT)	£1,000,000
Association of District Councils Debenture (ADC)	£50,000
Longer term investments (expiring in April 2007)	£3,000,000
Total Non-specified Investments	**£4,050,000**
Short Term Investments	
Investments	£30,000,000
BoS Instant Access Rate Account	£1,943,000
Total Short Term Investments	**£31,943,000**

3 Investment Strategy

3.1 Under Section 15(1)(a) of the Local Government Act 2003 every local authority is required, before the start of each financial year, to draw up an Annual Investment Strategy for the following financial year.

3.2 For this investment strategy the Council's priority is geared to the security and liquidity of its investments, although the yield is also a key consideration. The Council maintains only cash flow investments that are not generally considered appropriate for longer term investment. All its investment balances will therefore normally be maintained as short term or specified investments, with the exception of the LAMIT and ADC investments noted in Section 2 above.

3.3 As a contingency an upper limit allowing for up to £10 million to be invested for periods longer than 364 days is set as one of the prudential indicators for 2007/08 (see paragraph 6.1 (e) below). In line with this the minimum amount to be held during the year in investments other than long-term investments is 80% of the City Council's overall investments.

3.4 An investment is a specified investment if it satisfies the following conditions:

(i) The investment is denominated in sterling (see TMP1 – section 3)

(ii) The investment is not a long term investment (364 days or less)

(iii) The investment does not involve the acquisition of share capital or loan capital in any body corporate

(iv) All investments will be made with the UK Government or a local authority, or made with a body with a high credit rating as set out in the third schedule to *TMP4 – Approved Instruments, Methods and Techniques*.

3.5 There are no plans at present to make any non-specified investments in 2007/08, after the first two noted in Section 2 above have been repaid. However, any use of the other non-specified investments in Section 2 or an increase in longer term investments will be subject to the Council's liquidity requirements and be limited by the investment prudential indicator in 6.1 (e) below.

4 Prospects for Interest Rates

4.1 The Bank Base Rate increased to 5.00% in November 2006 and remained at that level throughout the rest of 2006. However, in January 2007, contrary to expectations, it was increased to 5.25%.

4.2 The current forecast is that a further increase cannot be ruled out in 2007 but, in view of the uncertainties surrounding this, it has not been considered prudent to factor this into future budgets.

5 External Debt

5.1 The Council repaid all external debt to become debt free in March 2002.

5.2 The strategy for external debt is to continue as a debt-free authority and to borrow only on a short-term basis to cover temporary shortfalls in cash. For this reason a maximum of £7 million has been set for external borrowing, although the operational boundary is set at £2 million. The need to borrow to fund the Council's capital programme will be kept under review, principally in the light of any changes to Government financing policy which may affect the position and having regard to the Council's future capital plans.

5.3 There is one long term liability of £74,000 which arises from a credit arrangement made with the contractor managing River Park Leisure Centre. However, the authorised limit has been set at £2 million in case other credit arrangements need to be entered into.

6 Prudential Indicators

6.1 The following treasury management prudential indicators are set for 2007/08:

a) The City Council has adopted the CIPFA Code of Practice for Treasury Management in the Public Services.

b) The upper limits on fixed interest rate and variable interest rate exposures are set at 100% for fixed rate and 20% for variable rate exposure.

c) Upper and lower limits for the maturity structure of borrowings – the upper limit is set at 100% for under 12 months, 100% for between 12 and 59 months and 100% for 5 years and above – the lower limit is set at 0% for periods up to 5 years and 0% for periods of 5 years and above.

d) The authorised limit for borrowing is set at £7 million, including £2 million for other long term liabilities with an operational boundary of £2 million.

e) Upper limit for principal sums invested for periods longer than 364 days is set at £10 million.

f) The minimum amount to be held during the year in investments other than long-term investments is set at 80% of the City Council's overall investments.

7 Performance Indicators

7.1 The following treasury management performance indicators are set for 2007/08:

a) Average rate earned on investments to be 0.1% above LIBOR 7 day market rate.

b) Investment management costs to be lower than the average for the CIPFA benchmarking club.

7.2 The results of these indicators will be reported in the annual Treasury Management Stewardship Report.