

CABINET

16 JULY 2003

TREASURY MANAGEMENT

REPORT OF THE DIRECTOR OF FINANCE

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RECENT REFERENCES:

CAB320: CIPFA Prudential Code for Capital Finance - 21 May 2003

CAB542: Treasury Management - 12 February 2003

EXECUTIVE SUMMARY:

This report sets out the detailed Treasury Management Practices (TMPs) that are required to be approved as part of the Council's Treasury Management policy in accordance with the CIPFA Code of Practice on Treasury Management.

RECOMMENDATIONS:

1. That Cabinet approves the Treasury Management Practices TMP1-12.

CABINET16 JULY 2003TREASURY MANAGEMENTREPORT OF THE DIRECTOR OF FINANCE1 Introduction

1.1 The City Council has adopted the key recommendations of CIPFA's Code of Practice for Treasury Management in the Public Services (Financial Procedure Rule 5.4).

1.2 This entails a commitment to adopt suitable treasury management practices setting out the manner in which the Council will seek to achieve its treasury management policies and objectives, and prescribing how it will manage and control those activities (Financial Procedure Rule 5.5).

2 Treasury Management Practices (TMPs)

2.1 The CIPFA Code of Practice on Treasury Management in the Public Services identifies a number of TMPs, all of which are recommended for adoption by the City Council and will be included in the Council's Treasury Management Manual.

2.2 The TMPs 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, and 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.

2.3 The wording of the TMPs is based on CIPFA guidance in the Code of Practice.

OTHER CONSIDERATIONS:3 CORPORATE STRATEGY (RELEVANCE TO):

3.1 Determination of the TMPs had regard to the key priority of maintaining budget stability through strong performance and resource management.

4 RESOURCE IMPLICATIONS: NoneBACKGROUND DOCUMENTS:

Operational and financial records held in the Finance Department and by other Departments.

CIPFA Code of Practice on Treasury Management in the Public Services.

APPENDICES: TMP1 to TMP12

TMP1 – RISK MANAGEMENT

Winchester City Council believes that the effective identification, monitoring and control of risk is a common and overriding aim of its treasury management policies. The following sections of this TMP identify type of risk and set out the ways in which the Council will monitor and control those risks.

1. **Liquidity Risk**

The risk that cash will not be available when it is needed, that ineffective management of liquidity creates additional unbudgeted costs, and that the Council's service objectives will be thereby compromised.

The Council will ensure that 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 service objectives.

The Council will maintain an effective cash and cashflow forecasting and monitoring system that will identify the extent to which the Council is exposed to the effects of potential cashflow variations and shortfalls. The principles of this system are set out in *TMP8 – Cash and Cashflow Management*.

2. **Interest Rate Risk**

The risk that fluctuations in the levels of interest rates create an unexpected or unbudgeted burden on the Council's finances, against which the Council has failed to protect itself adequately.

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.

The Council will have regard to professional advice on the likely future course of interest rates to enable it to assess the extent to which movements in these may impact on the Council. Appropriate procedures are built into the Council's budget processes to enable this to happen and commentary will be included in the annual treasury management strategy.

3. **Exchange Rate Risk**

The risk that fluctuations in foreign exchange rates create an unexpected or unbudgeted burden on the Council's finances, against which the Council has failed to protect itself adequately.

Council policy is to conduct its affairs in sterling, thereby avoiding any exposure to exchange rate fluctuations.

4. **Inflation Risk**

The risk that prevailing levels of inflation cause an unexpected or unbudgeted burden on the Council's finances, against which the Council has failed to protect itself adequately.

The Council will have regard to professional sources and advice on the likely future course of inflation to enable it to assess the extent to which changes may impact on the Council. Appropriate procedures are built into the Council's budget processes to enable this to happen.

5. **Credit and Counterparty Risk**

The risk of failure by a third party to meet its contractual obligations to the Council under an investment, borrowing, capital, project or partnership financing, particularly as a result of the third party's diminished creditworthiness, and the resulting detrimental effect on the Council's capital or revenue resources.

The Council regards a prime objective of its treasury management activities to be the security of the principal sums it invests. Accordingly, it 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* and listed in the schedule included in that document. 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 other financing arrangements.

The Council operates a policy of diversification in the organisations it deals with for borrowing and investment in order to avoid over reliance on a small number of third parties. The standing and status of these third parties is kept under continuous review with professional advisors and subscription services.

6. Refinancing Risk

The risk that maturing borrowings, capital, project or partnership financing cannot be refinanced on terms that reflect the provisions made by the Council for those refinancings, both capital and revenue, and/or that the terms are inconsistent with prevailing market conditions at the time.

The Council is currently debt free but will ensure that any future 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 Council as can reasonably be achieved in the light of market conditions prevailing at the time.

The Council 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

The risk that the Council itself, or a third party with which it is dealing in its treasury management activities, fails to act in accordance with its legal powers or regulatory requirements, and that the Council suffers loss accordingly.

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[5] 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 Council, 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 reasonable 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 risk that the Council fails to identify the circumstances in which it may be exposed to the risk of loss through fraud, error, corruption or other eventualities in treasury management dealings, and fails to employ suitable systems and procedures and maintain effective contingency management arrangements to these ends. It includes the area of risk commonly referred to as operational risk.

The Council will ensure that it has identified the circumstances that 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

The risk that, through adverse market fluctuations in the value of the principal sums the Council invests, its stated treasury management policies and objectives are compromised, against which effects it has failed to protect itself adequately. This 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 sums it invests, and will accordingly seek to protect itself from the effects of such fluctuations.

Finance will only be raised in accordance with the Local Government and Housing Act 1989 or subsequent authorising legislation.

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TMP2 – BEST VALUE AND PERFORMANCE MEASUREMENT

This Council is committed to the pursuit of best value 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 stated business and service objectives. It will be the subject of regular examination of alternative methods of service delivery, of the availability of fiscal or other grant or subsidy incentives, and the scope for other potential improvements. The performance of the treasury management function will be measured using the criteria set out in the schedule to this document.

SCHEDULE

1 Performance measures and targets

Investments

- ❖ Average return on investments to exceed the sterling interbank rate

Borrowing

- ❖ To remain debt free whilst it is financially advantageous for the Council to be so

2 Benchmarking

The Council will benchmark its costs and performance in carrying out the treasury management function against those of other local authorities. The target is to be in the lower quartile for costs of service with peer authorities.

TMP3 – DECISION-MAKING AND ANALYSIS

This 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. The issues to be addressed and practices to be pursued in reaching decisions are detailed in the schedule to this document.

SCHEDULE

Records

- Cashflow spreadsheets
- Investment spreadsheets
- Investment ledger
- Transaction files
- Bankline records
- Bank statements
- Committee reports

Processes

- Temporary loans – lending
- Temporary loans – repayment
- Treasury deposits
- Bankline – balances
- Bankline – transfers
- Bankline – electronic payments

Issues

Economic and market factors will be evaluated on a regular basis, taking external expert advice as necessary, to ensure that the merits, manner and timing of treasury management activity are appropriate.

Documentation and systems will be reviewed on a regular basis to ensure that they are adequate to meet the treasury management needs of the Council.

TMP4 – APPROVED INSTRUMENTS, METHODS AND TECHNIQUES

This Council will undertake its treasury management activities by employing only those instruments, methods and techniques detailed in the schedule to this document and within the limits and parameters defined in TMP1 *Risk Management*.

SCHEDULE

1 Approved Instruments

The following list specifies which borrowing instruments can be adopted:-

- ❖ Public Works Loan Board
- ❖ Market Long-term
- ❖ Market Temporary
- ❖ Local Bonds
- ❖ Local Temporary
- ❖ Overdraft
- ❖ Negotiable Bonds
- ❖ Stock Issues
- ❖ Leasing
- ❖ Internal (capital receipts and revenue balances)

All the above forms of funding may be considered, depending on the prevailing economic climate, regulations and local considerations. The Director of Finance shall have delegated powers to take the most appropriate form of borrowing from the approved sources.

Should new instruments become available or should the Council consider using an instrument for the first time, the tests of legality, objectivity, suitability, risks, costs and status of counterparty will be applied before Council approval is sought to their use.

2 Approved Methods and Techniques

The range of approved methods to be used in the process of treasury management shall include trained internal staff resources and advice from authorised consultants, brokers and bankers.

Internal staff resources will maintain relevant skills through appropriate training and CPD (Continuing Professional Development) activities.

The use of authorised treasury management consultants, authorised brokers and banking facilities will be subject to periodic market testing (as per TMP1) and competency standards.

No novel techniques will be introduced without full evaluation and an assessment of all consequences for the Council.

TMP5 – ORGANISATION, CLARITY AND SEGREGATION OF RESPONSIBILITIES, AND DEALING ARRANGEMENTS

This 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 the Council intends, as a result of lack of resources or other circumstances, to depart from these principles, the Director of Finance 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 Director of Finance 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 present arrangements are detailed in the schedule to this document.

The delegations to the Director of Finance in respect of treasury management are set out in Section 5.7 of the Council's Financial Procedure Rules. The Director of Finance 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*.

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TMP6 – REPORTING REQUIREMENTS AND MANAGEMENT INFORMATION ARRANGEMENTS

This 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 these policies; on the implication 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, the Council will receive:

- an annual report on the strategy and plan to be pursued in the coming year
- an annual report on the performance of the treasury management function, on the effects of decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the Council's treasury management policy statement and TMPs.

The present arrangements for these reports are detailed in the schedule to this document.

SCHEDULE

- ◆ The Treasury Management Strategy Report for the ensuing financial year will go to Cabinet in mid February each year and then to Council for approval at the end of February each year.

- ◆ The Treasury Management Stewardship Report will go to Cabinet in September each year.
- ◆ Any ad hoc treasury management reports needed under the Code of Practice will be considered by Cabinet at the earliest opportunity.
- ◆ All Treasury Management reports will be considered by Corporate Management Team before going to Cabinet.

A monthly transactions report will be considered by the Director of Finance

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TMP7 – BUDGETING, ACCOUNTING AND AUDIT ARRANGEMENTS

The Director of Finance will prepare, and the 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*, TMP2 *Best value and performance management*, and TMP4 *Approved instruments, methods and techniques*. The form which the Council's budget will take is set out in the Council's annual Budget Book. The Director of Finance will exercise effective controls over this budget, and will report upon and recommend any changes required in accordance with TMP6 *Reporting requirements and management of information arrangements*.

This 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. The present form of the Council's accounts is set out in the Statement of Accounts published each year.

This Council will ensure that its auditors, and those charged with regulatory review, have access to all information and papers supporting the activities of the treasury management function as are necessary for the proper fulfilment of their roles, and that such information and papers demonstrate compliance with external and internal policies and approved practices.

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TMP8 – CASH AND CASH FLOW MANAGEMENT

Unless statutory or regulatory requirements demand otherwise, all monies in the hands of this Council will be under the control of the responsible 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 responsible officer will ensure that these are adequate for the purpose of monitoring compliance with TMP1[1] *liquidity and risk management*. The present arrangements for preparing cash flow projections, and their form, are set out in the schedule to this document.

SCHEDULE

1. The Authority's cash balances are monitored in order to ensure that demand for cash can always be met and that large cash balances are used effectively.
2. A cashflow schedule is kept on a spreadsheet of expected bank transactions, a separate page relates to each complete month and shows income and expenditure on the Council's Drawings, General and Community Charge bank accounts.

3. Bank balances are extracted from the Bankline system on a daily basis. Large balances (over about £250,000) for investment will be invested with approved organisations and timed to be repaid to coincide with large payments out. The limit on the amount to be invested with any individual borrower will be observed. Similarly, if borrowing is necessary, repayment dates will coincide with expected income flows.
4. After the day's business has been completed if the Drawings account is near to £1m overdrawn, or will be after transactions on the day, a transfer between the accounts will be done using the Bankline system.
5. The Assistant Accountant will make the necessary transactions on Bankline and the entries to the spreadsheet. The Chief Accountant will monitor the validity of the bank transactions and that the spreadsheet is kept current.

The form of the spreadsheet is shown as an attachment to this schedule and is maintained in the Accountancy folder on the Finance Department server.

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TMP9 – MONEY LAUNDERING

This 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.

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TMP10 – STAFF TRAINING AND QUALIFICATIONS

This 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 Director of Finance will implement the necessary arrangements.

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TMP11 – USE OF EXTERNAL SERVICE PROVIDERS

This Council recognises the potential value of 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 ensure it does so for reasons which will have been submitted to a full evaluation of the costs and benefits. It will also ensure that the terms of the appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review. And it will ensure, where feasible and necessary, that a spread of service providers is used, to avoid overreliance on one or a small number of companies. 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 responsible officer and details of current arrangements are set out in the schedule to this document.

SCHEDULE

<u>Service</u>	<u>Provider</u>	<u>Start date</u>	<u>Period</u>
Banking Services	National Westminster	April 2002	3 years (option +2)
TM Advice	Butlers	February 2003	2 years
Brokerage Services	Tradition UK) Sterling Brokers) Garban Intercapital) Tullett & Tokyo) NatWest Bank)) London Money Market brokers) ongoing and used as required	
Bank Tender Advice	Focus on Banking	July 2001	N/A

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TMP12 – CORPORATE GOVERNANCE

This Council is committed to the pursuit of proper corporate governance throughout its businesses and services, and to establishing its 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 Council has adopted and implemented the key recommendations of the CIPFA Code of Practice. This is considered vital to the achievement of proper corporate governance in treasury management, and the Director of Finance will monitor and, as and when necessary, report upon the effectiveness of these arrangements.

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