

Report to: **Audit Committee**

Date of Meeting: **13 March 2013**

Report of: **Head of Strategic Finance**

Title: **Treasury Management Annual Review**

1.0 SUMMARY

- 1.1 To inform Members of the Treasury Management Annual Report and Prudential Indicators for 2011/12; to present to Members a mid year review of the Treasury Management function in 2012/13; and to report the Treasury Management Strategy for 2013/14 – 2015/16.

2.0 RECOMMENDATIONS

- 2.1 That the Committee notes the Treasury Management Annual Report 2011/12; the Mid Year Treasury Management Monitoring Report 2012/2013, the Treasury Management Strategy Statement 2013/14 – 2015/16 and the Treasury Management Practice guidance..
- 2.2 The Audit Committee is specifically recommended to approve Appendix 3, the Treasury Management Strategy Statement, and refer it to Council for approval.

3.0 SALIENT ISSUES

- 3.1 This report has a similar problem to the Statutory Statement of Accounts namely that it is largely incomprehensible to a lay person but regrettably has to be followed as it is a format devised by professional 'experts', the Chartered Institute of Public Finance and Accountancy (CIPFA) and has been expanded by the Council's Treasury adviser, Sector (and will be widely adopted by most local authorities).
- 3.2 This "introduction" attempts to draw out the key issues reflected within subsequent sections of this report.
- 3.3 **Appendix 1** formally reviews the Council's activities / performance during 2011/2012 and has been reported previously in regular reports to the Audit Committee. It confirms the Council did not incur any external debt, only invested with approved counterparties, and outperformed the investment return benchmark.
- 3.4 **Appendix 2** reports upon the half year treasury management activities / performance and has again been reported to Audit Committee (in a more concise form) at its meeting on 25 September 2012. It again reports no external debt, investments only with approved Counterparties; a forecast investment rate of return of 1.15% (original estimate 1.30%); and an expectation that £325k of cash will accrue on our investments (as per Original estimate).
- 3.5 **Appendix 3** is the most interesting part of the report and details the parameters for borrowing and investments within which officers are required to operate. In essence it recommends the ability to borrow up to a maximum of £10m and reflects anticipated borrowing of £6m from the Herts Local Enterprise Partnership Growing Places Fund and further potential funding for other re-development projects. In all cases there will be an expectation that a financial return will accrue to enable these loans to be repaid within a relatively short period of time. Appendix 3 also details the criteria for determining to whom the Council should be lending its money and has been reviewed in the light of the general credit rating downgrades that have occurred over the past twelve months.

3.6 **Appendix 4** reports upon the Treasury Management Practice (TMP1) - Credit and Counterparty Risk Management guidance.

4.0 There is no section 4 to this report (late re-numbering !)

5.0 DETAILED EXPLANATION OF THE TREASURY MANAGEMENT REPORTS

5.1.1 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."

5.1.2 The reports meet the requirements of CIPFA's Code of Practice on Treasury Management and the CIPFA Prudential Code for Capital Finance in Local Authorities and complies with the Local Government Act 2003.

5.2 Treasury Management Annual Report and Actual Prudential Indicators 2011/12 (Appendix 1)

5.2.1 This report provides details of actual prudential and treasury indicators and treasury operations during 2011/12 compared to the estimates within the strategy. The report is made in line with the Council's approved policy on Treasury Management.

5.2.2 During 2011/12, the Council complied with its legislative and regulatory requirements and the Head of Strategic Finance confirms that the statutory borrowing limit (the authorised limit), was not breached.

5.2.3 The financial year 2011/12 continued the challenging environment of previous years; low investment returns and continuing counterparty risk.

5.2.4 The Head of Strategic Finance also confirms that no borrowing was undertaken. At 31 March 2012, the Council had no external debt and its investments totalled £29.112m (£31.874m at 31 March 2011).

5.2.5 This report contains:

- Capital activity during the year;
- Reporting of the required prudential and treasury indicators;
- Impact of this activity on the Council's underlying indebtedness (the Capital Financing Requirement);
- Overall treasury position and the impact on investment balances;
- Summary of the economy and interest rates;
- Investment Rates in 2011/12;
- Investment Outturn for 2011/12.

5.3 Mid Year Treasury Management Monitoring Report (Appendix 2)

5.3.1 This report updates members upon the progress of the capital financing, amending prudential indicators as necessary, and whether the treasury strategy is being met or any policies require revision.

5.3.2 The underlying economic environment remains difficult for the Council, foremost being the concerns over investment counterparty risk. This background encourages the Council to continue maintaining investments short term and with high quality counterparties. The downside of such a policy is that investment returns remain low.

5.3.3 The basis of the treasury management strategy, the investment strategy and the performance indicators are not changed.

5.3.4 The prudential code requires the Council to update:

- The Council's capital expenditure plans;
- How these plans are being financed.

These requirements are met by the Council's Budget Monitoring & Reporting Framework, which includes revised capital expenditure and funding statements within the Budget Book.

5.4 Treasury Management Strategy Statement 2013/14 – 2015/16 (Appendix 3)

5.4.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the 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 medium risk appetite, providing adequate liquidity initially before considering investment returns.

5.4.2 This report covers two main areas:

Capital Issues

- The capital plans 2013/14 – 2015/16;
- The Minimum Revenue Provision strategy and policy statement.
- The long and short term borrowing requirement

Treasury Management Issues

- The current portfolio position;
- Treasury indicators: limits to borrowing activity;
- Prospects for interest rates;
- The borrowing strategy;
- Annual investment strategy;
- Reporting requirements;
- Policy on use of external service providers; and
- Member and officer training.

5.4.3 The Treasury Management Policy Statement, details the policies, practices, objectives and approaches to risk management of its treasury management activities and has previously been adopted by the Audit Committee. There are no changes to the Treasury Management Policy Statement to report and the treasury service confirm that they are complying with all aspects of the the Treasury Policy Statement and will continue to comply in future years.

5.4.4 It should be noted however that the criteria for placing investments have been reviewed to take into account general credit rating adjustments that have occurred over the past twelve months.

5.4.5 It is necessary for Council to agree the degree of risk to which it is prepared to expose the investment portfolio. The Head of Strategic Finance would define this as follows:

- Low Risk—limited to use of the Debt Management Office facility and other UK sovereign financial instruments; major clearing banks possessing high credit rating (or substantially owned by the UK Government); triple AAA money market funds; local authorities.
- Medium Risk—the use of Building Societies with an asset base above £5,000m as this sector is generally not rated by the Credit Rating Agencies;
- High Risk—low rated clearing banks; banks based outside the UK (this is a generalisation as many German / Dutch / Scandinavian and French banks would almost certainly be deemed too big to fail); building societies having a small asset base.

5.4.6 By the above 'crude' criteria, Watford might be considered to have a medium appetite for risk and the Audit Committee and Council will need to feel comfortable with this approach.

6.0. IMPLICATIONS

6.1 Financial

6.1.1 The Head of Strategic Finance comments that the Treasury Management Statements have no direct financial implications although Appendix 3 does, in particular, set parameters within which officers should operate and could result in indirect financial implications which are not possible to evaluate at this time.

6.2 Legal Issues (Monitoring Officer)

6.2.1 The Head of Legal and Property Services comments that it is a statutory requirement that the Treasury Management Strategy and Treasury Management Practices are reviewed annually.

6.3 Potential Risks

Potential Risk	Likelihood	Impact	Overall Score
That the Council will exceed its borrowing parameters	1	3	3
That the Council will be unable to service its annual borrowing costs	1	3	3
That the Council will be unable to repay any loans at maturity date	1	4	4
Investment placed with a non approved body	1	3	3
Investment with a counterparty that subsequently defaults	1	4	4

Background papers:

UK Economic Forecasts provided by Sector, the Council's treasury advisors;
 CIPFA Prudential Code for Capital Finance in Local Authorities, 2011 Edition;
 CIPFA Treasury Management in the Public Services – Code of Practice and Cross-Sectoral Guidance Notes, 2011 Edition;
 CIPFA Treasury Management in the Public Services, Guidance Notes for Local Authorities, 2011 Edition;
 Outturn figures from E Financials, Logotech Treasury Management and Statement of Accounts.

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