

Accounts, Audit and Risk Committee

2012/13 Treasury Management Strategy and Update on Performance

19 March 2012

Report of the Head of Finance and Procurement

PURPOSE OF REPORT

The report provides a review of the 2012/13 strategy that was approved by Council on 27 February 2012 and outlines the differences from the current 2011/12 strategy, and gives an update on current performance.

This report is public

Recommendations

The Accounts, Audit and Risk Committee is recommended:

- (1) To note the contents of the report.

Executive Summary

- 1.1 As part of our investment strategy and governance arrangements this committee considers the investment performance and our compliance with counterparties being used.
- 1.2 The Code of Practice on Treasury Management approved by the Chartered Institute of Public Finance and Accountancy (CIPFA) and adopted in full by the Council in 2004, requires that a Treasury Management Strategy is produced prior to the beginning of the financial year to which it relates. The Treasury Management Strategy is the cornerstone of proper treasury management, and is central to the operation, management reporting and performance assessment. This strategy was approved by Council on 27 February 2012.
- 1.3 The highest standard of stewardship of public funds remains of the utmost importance to the Council. This document sets out the Council's priorities and policies for making, and managing investments made by the Council in the course of undertaking treasury management activities during the 2011/12 financial year.

Background Information

Treasury Performance and 2012/13 Treasury Strategy

- 2.1 The Council has £11.5m and £11.6m respectively invested with fund managers Tradition UK and Investec. In addition it has around £56.7m managed in-house (including Eco Town funds of £11.5m) which fluctuates during the year.
- 2.2 These funds are currently invested in accordance with the 2011/12 strategy and there have been no breaches of this policy.
- 2.3 The Treasury Management Strategy is the cornerstone of proper treasury management, and is central to the operation, management reporting and performance assessment.
- 2.4 The proposed strategy for 2012/13 is attached in Appendix 1 and is based upon the views of the Chief Financial Officer, Head of Finance and Procurement and the Council's Treasury Management Team. This is informed by market forecasts provided by the Council's treasury advisor, Sector.
- 2.5 In consultation with Sector and with full reference to the CIPFA Code of Practice, the Council has reviewed its risk appetite and associated priorities in relation to security, liquidity and yield in respect of returns from various financial instruments.
- 2.6 The strategy detailed in Appendix 1 covers:
 - The Current Treasury Position
 - Prospects for interest rates
 - The borrowing strategy
 - Prudential Indicators
 - The investment strategy
 - Creditworthiness policy
 - Policy on use of external service providers.
- 2.7 There are 3 main changes to the 2011/12 strategy:
 - revised CIPFA Treasury Management Code of Practice 2011
 - revised CIPFA Prudential Code 2011
 - a number of downgrades to counterparty ratings

The Revised CIPFA Treasury Management Code of Practice 2011

- 2.8 The revised Code has emphasised a number of key areas including the following:-
- 2.9 CIPFA revised the Treasury Management Code of Practice (TM Code) and associated Guidance Notes in November 2011. This revision is an update to the Treasury Management Code and Guidance Notes last published in November 2009.

- 2.10 The TM Code has been reviewed and updated following recent developments and anticipated regulatory changes relating to the Localism Bill 2011, including housing finance reform and the introduction of the General Power of Competence.
- 2.11 The new TM Code contains an expansion of the risk management chapter. (There is also now a new chapter covering the treasury management implications of the housing reform which is not applicable to this Council as it no longer has housing stock.)
- 2.12 This document sets out the principal changes to the TM Code and associated Guidance Notes, and outlines the impact this could have on Councils' Treasury Management Strategy Statements. Key changes are as follows:
- Authorities are to explicitly state in their TMSS whether they plan to use derivative instruments to manage risks, and ensure they have the legal power to do so
 - Authorities are to make reference to their high level approach to borrowing and investment in their Treasury Management Policy Statement
 - Less focus is placed on the 'minimum credit limits' for investment counterparties, with more focus on the 'minimum acceptable credit quality'
 - There is a New treasury indicator: Upper limits on the proportion of net debt to gross debt; to highlight where an authority may be borrowing in advance of its cash requirement
 - Authorities may wish to create a new treasury indicator which considers credit risk
 - Expansion of the risk management chapter
 - New Section in the TM Code Guidance Notes on the 'Treasury Management Implications of the Housing Self-Financing Reform' – this is not applicable to this Council.
- 2.13 This strategy statement has been prepared in accordance with the revised Code. Accordingly, the Council's Treasury Management Strategy will be considered for approval annually by the full Council and there will also be a mid year report.
- 2.14 In addition there will be monitoring reports and regular review by members in both executive and scrutiny functions.
- 2.15 The aim of these reporting arrangements is to ensure that those with 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 relating to delegation and reporting.
- 2.16 This Council adopts the reporting arrangements outlined in Annex 1 of Appendix 3 which is in accordance with the requirements of the revised Code.

The Revised CIPFA Prudential Code

- 2.17 CIPFA has issued a revised Prudential Code which primarily covers borrowing

and the Prudential Indicators. (Three of these indicators are classified as Treasury Indicators rather than Prudential Indicators):

- Actual External Debt
- Gross and net debt
- Interest rate exposures
- Maturity structure of borrowing
- Principal sums invested for periods longer than 364 days
- Credit risk.

(All indicators are presented together as a suite of indicators in Annex 1 of Appendix 3)

Counterparty Ratings

- 2.18 Following on from advice received by our Treasury Advisors, the Council will select financial institutions with a minimum long-term rating of A and short-term rating of F1/P-1/A-1. There may be occasions when the counterparty ratings from one rating agency are marginally lower than these ratings but may still be used. In these instances consideration will be given to the whole range of ratings available, or other topical market information, to support their use.
- 2.19 The long-term rating of A is lower than the minimum of A+ adopted in 2011/12 and is in response to downgrades in the autumn of 2011 to the ratings of many institutions considered to be systemically important. The downgrades did not reflect deterioration in the financial strength of the UK government or the financial system; rather they were a result of the agencies' assessment that the various policy recommendations of the Independent Commission on Banking will most likely result in extraordinary government support for financial institutions being relatively lower and less certain than before.
- 2.20 The Council will also assess other indicators, such as credit default swaps, share prices, the sovereign's economic fundamentals, corporate developments highlighted through news articles and market sentiment. If any of these indicators give rise to concern, the counterparty may be suspended from further use irrespective of the existing credit rating.
- 2.21 The highest standard of stewardship of public funds remains of the upmost importance to the Council. This strategy sets out the Council's priorities and policies for making, and managing investments made by the Council in the course of undertaking treasury management activities during the forthcoming 2012/13 financial year.

Investment Income / Icelandic Banks

- 2.22 At the closure of the 2010/11 accounts the Council had assumed a prudent position with regard its Icelandic investments, accounting for a loss in value of its investment portfolio (known as impairment) until the challenge to priority creditor status at the court of appeal was resolved.

- 2.23 Following appeal, the Council was awarded priority creditor status for its Icelandic investments with Glitnir - total £6.5m and this decision is now final.
- 2.24 Consequently, it is anticipated there will be a complete repayment of the £6.5m due from Glitnir Bank before the 31 March 2012. In accounting terms the loss shown last year will be reversed and the average cash position available for investment that has been budgeted will improve. The latest position will be given at the meeting.
- 2.25 The Council's investment income budget for 2012/13 has been compiled on the basis of close tracking of actual and likely interest rates and with the help of external advice. The emphasis has been on the least risky places to invest the Council's money and this, along with the continued low interest rates on offer and the agreed use of capital receipts has led to a significant reduction in the investment income built into the budget. In budgetary terms this is prudent and places the Council at less risk of exposure in-year.

Key Issues for Consideration/Reasons for Decision and Options

The following options have been identified. The approach in the recommendations is believed to be the best way forward.

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| Option One | Agree the recommendations |
| Option Two | To approve or reject the recommendations above or request that Officers provide additional information. |

Consultations

None

Implications

Financial: This report has no specific financial implications. The budget monitoring reports consider investment returns on a monthly basis.

Comments checked by Karen Muir, Corporate System Accountant, 01295 221559.

Legal: There is a requirement for the Council to fulfil two key requirements of the Local Government Act 2003:-

- approval of the Treasury Management Policy in accordance with the CIPFA Code of Practice on Treasury Management
- approval of the Investment Strategy in accordance with the DCLG investment guidance.

Comments checked by Kevin Lane, Head of Law and Governance, 0300 0030107.

Risk Management:

- Risk of capital loss – the prime objective of treasury management activities is to ensure the security of the amounts invested. This is managed by using a counterparty list which only includes organisations having a suitable credit rating and which has a

maximum amount that can be invested with each organisation at any one time.

- Liquidity – investments are linked to known future cash flows to ensure sufficient funds are available as and when they are required.
- Interest Receivable – this is regularly monitored against budget and reported through the Performance management Framework.

Comments checked by Karen Muir, Corporate System Accountant, 01295 221559.

Wards Affected

All

Corporate Plan Themes

An Accessible and Value for Money Council

Executive Portfolio

Councillor Ken Atack
Lead Member Financial Management

Document Information

Appendix No	Title
Appendix 1	2012/13 Strategy
Background Papers	
2011/12 Budget Monitoring Reports and dashboard Sector TMSS template Local Government Act 2003 CIPFA's revised Prudential Code for Capital Finance in Local Authorities CIPFA's revised Treasury Management Code of Practice Prudential Indicator working files Capital Programme 2011-2016 Medium Term Financial Strategy 2012/13 Budget Booklet	
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