Appendices: 4

Appendix 1

NORTHAMPTON
BOROUGH COUNCIL

COUNCIL
10 September 2012

Agenda Status: Public **Directorate: Finance & Support**

Report Title	TREASURY MANAGEMENT OUTTURN 2011-12

1. Summary

1.1 The purpose of the report is to inform Council of performance in relation to its borrowing and investment strategy for 2011-12.

2. Recommendations

2.1 That Council note the Council's treasury management performance for 2011-12.

3. Report Background

3.1 **CIPFA Code of Practice on Treasury Management in the Public Services**

3.1.1 The Council has adopted the CIPFA Code of Practice on Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes ("the Treasury Management Code of Practice").

3.1.2 The Treasury Management Code of Practice includes recommendations on annual reporting requirements after the year-end. The table below shows how these have been incorporated into this report.

Reporting Requirement	Reference
Report on the risk implications of decisions taken and transactions executed	Paragraph 3.2.6
Transactions executed and their revenue (current) effects	Paragraph 3.2.7 to 3.2.10 Appendix B
Performance report	Paragraph 3.2.7 to 3.2.10 Appendix B
Monitoring of treasury management indicators for local authorities.	Paragraph 3.2.11 Appendix C
Compliance report on agreed policies/practices and on statutory/regulatory requirements	Paragraph 3.2.12 to 3.2.13
Report on compliance with CIPFA Code recommendations	Paragraph 3.2.14

3.2 Issues

Accounting & Audit Issues

3.2.1 The CIPFA Code of Practice on Local Authority Accounting includes a complex set of regulations on accounting for financial instruments. These requirements have been fully complied with in the preparation of the Council's Statement of Accounts.

3.2.2 The regulations include the values at which financial instruments, including borrowing and investments, should be calculated for inclusion on the balance sheet at year-end. In some instances, this is at amortised cost, whereby the balance sheet value is written up or down via the comprehensive income and expenditure account over the life of the instrument to reflect costs or benefits, such as transaction costs or interest earned or due to date. Alternatively, financial instruments may be valued at their original cash value.

3.2.3 In summary, and broadly speaking, the balance sheet values of the Council's debt and investments at 31 March 2012 are shown in the following ways:

Borrowing (Financial Liabilities)	
Long term borrowing	Amortised cost
Short term borrowing	Original (cash) value
Investments (Financial Assets)	
Deposit and call accounts (cash equivalents)	Original (cash) value
Money market funds (cash equivalents)	Original (cash) value
Short term money market investments up to three months duration (cash equivalents)	Original (cash) value
Short term money market investments over three months duration	Amortised cost

3.2.3 Outturn figures relating to borrowing and investments are shown and discussed at paragraphs 3.2.7 to 3.2.9 below. All outturn figures contained in this report are subject to external scrutiny, through the annual audit of the Council's Statement of Accounts.

Economic Environment and Interest Rates

3.2.5 2011-12 was another year of turbulence in the economic environment, most notably in the Euro zone. The trend of low interest rates has continued throughout the year, against a background of a Bank of England base rate that has remained unchanged at 0.5%. A short commentary on the economic environment and interest rates, provided by Sector, the Council's treasury management advisers, is included at **Appendix A1**. Definitions of the key terms used (Bank of England base rate, LIBID rate, LIBOR rate) and an analysis of interest rate movements in the year are included at **Appendix A2.**

Risk implications of decisions taken and transactions executed

3.2.6 The Treasury Management Code of Practice identifies eight main treasury management risks. Definitions of these are included in the Council's Treasury Management Practices (TMPs) for 2011-12 reported to Cabinet on 23 February 2011 and Council 28 February 2011. The management of these risks during 2011-12 is covered in the following paragraphs.

a) Credit and counterparty risk – In the economic and banking environment that prevailed during 2011-12, this continued to be an area of considerable risk for all local authority investors. The Council managed this risk extremely closely during the year through strict adherence to its treasury management policies and practices and a tightly controlled counterparty list that took into account a range of relevant factors including sovereign rating, credit ratings, inclusion in the UK banking system support package and credit default swap spreads. The advice of the Council's treasury management advisors was also an underlying feature. None of the Council's counterparties failed to meet their contractual obligations to the Council under treasury transactions during 2011-12.

b) Liquidity risk – This was managed effectively during 2011-12 through pro-active management of the Council's cashflow, including the choice of suitable investment values and maturity dates and the maintenance of sufficient levels of liquid cash in money market funds and deposit accounts. The Council also maintained its access to overdraft facilities and temporary borrowing facilities as a contingency for use in exceptional circumstances. The Council undertook no long or short-term borrowing to manage liquidity during 2011-12.

c) Interest rate risk - The Council's upper limits for fixed and variable interest rate exposures in respect of investments, borrowing and net external debt are managed as treasury indicators. These are reported at **Appendix C**. The indicators were not breached during 2011-12.

d) Exchange rate risk - The Council has a policy of only entering into loans and investments that are settled in £ sterling, and has no treasury management exposure to this category of risk.

e) Refinancing risk – The Council did not refinance any of its debt during 2011-12 and was therefore not exposed to this category of risk during the year.

f) Legal and regulatory risk - The Council has carried out its treasury management activities for 2011-12 within the current legal and regulatory framework. Officers responsible for strategic and operational treasury management decisions are required to keep abreast of new legislation and regulations impacting on the treasury management function, and have applied any changes as necessary. Legal and regulatory risks associated with other organisations with which the Council deals in its treasury management activities have been managed through counterparty risk management policies.

g) Fraud, error and corruption and contingency management - Officers involved in treasury management are explicitly required to follow treasury management policies and procedures when making investment and borrowing decisions on behalf of the Council. All treasury activities must be carried out in strict accordance with the agreed systems and procedures in order to prevent opportunities for fraud, error and corruption. The measures in place to ensure this include a scheme of delegation and segregation of duties, internal audit of the treasury function, detailed procedure notes for dealing and other treasury functions, and emergency and contingency planning arrangements (including a business continuity plan for treasury management). The internal auditors assessed the Council's treasury management as low risk in 2011-12.

h) Market risk – The Council did not hold any investments during 2011-12 that were subject to fluctuations in market value, such as gilts, CDs (Certificates of Deposit) and bonds, and was therefore not exposed to this category of risk during the year. However, the Council does have deposits placed in a Money Market Fund, whereby the underlying assets of the fund are subject to capital fluctuations. The movements in capital are as a result of interest rate risk and credit risk. The structure of the fund minimises the movement of capital value due to the restrictions laid down by the credit rating agencies.

Performance Report - Borrowing

3.2.7 Long Term Borrowing

a) The table below shows the Council's long-term debt as at 31 March 2012 at amortised cost. The total debt outstanding is £216m.

Long Term Debt Outstanding at 31 March 2012	**Principal**	**Proportion of Debt**	**Range of Interest Rates**	
			From	**To**
	£000	**%**	**%**	
PWLB	190,113	88	1.24	3.97
Money Market LOBO Loans	24,788	11	4.85	7.03
HCA Annuity Loan	1,191	1	9.25	9.25
Total	**216,092**	**100**		

b) New PWLB borrowing of £184m was undertaken on 28 March 2012, to fund the settlement payment of £193m to the Department of Communities and Local Government (DCLG) to buy out of the housing subsidy system. The balance of £9m was funded from an existing LOBO loan, which has been assigned to the HRA. The Council has adopted a two-pool approach to splitting debt between the HRA and General Fund, whereby both existing loans and new loans are assigned internally to either the HRA or the General Fund.

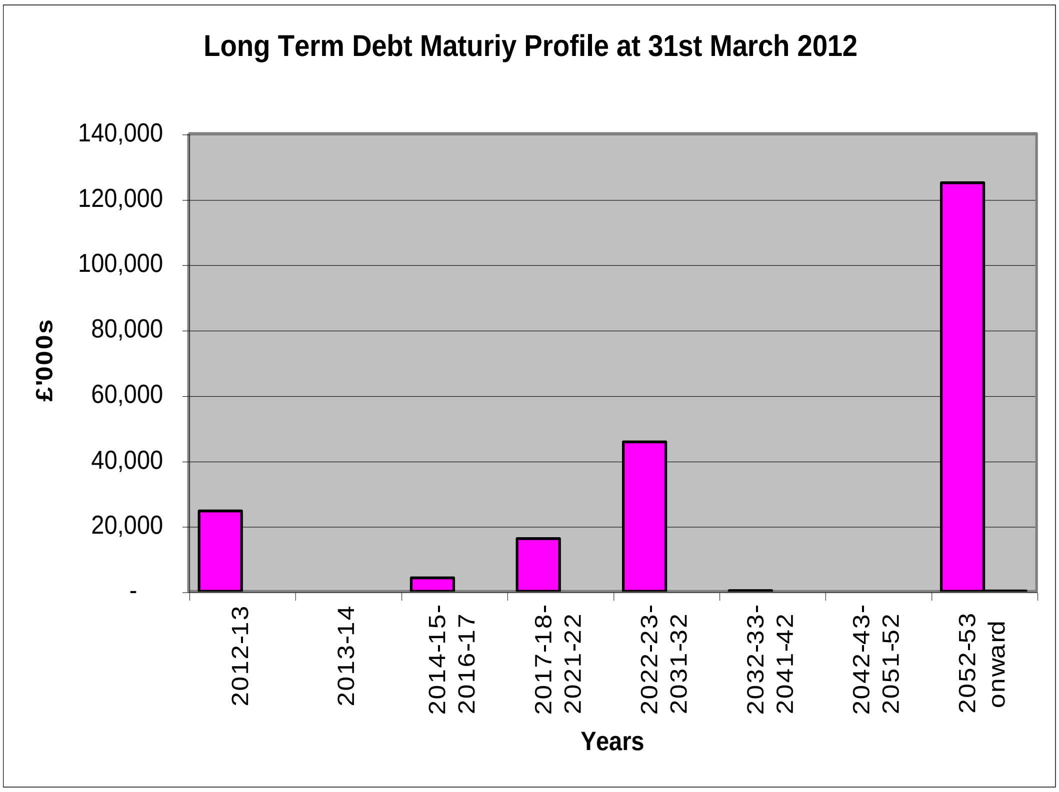
c) No loans were repaid during the year other than the scheduled repayment of the principal element of the annuity with the Homes and Communities Agency (HCA) (£17k) due in 2011-12. The principal amount due to HCA in 2012-13 (£19k) is treated as short-term borrowing and is included in the discussion at paragraph 3.2.8 below.

d) Under Section 3 of the Local Government Act 2003, the Council is required to set an annual affordable borrowing limit. This limit is also set as a prudential indicator, i.e. the authorised limit for external debt. Council agreed an amended affordable borrowing limit for 2011-12 on 24 October 2011, to cover the borrowing needed for HRA self-financing.

Compliance is demonstrated below:

	Affordable Borrowing Limit as set 24 October 2011	**Maximum Actual Amount Outstanding in Year**
Overall Borrowing	£265m	£216m

e) The graph below illustrates the Council's long-term debt maturity profile as at 31 March 2012. The figures are shown at original (cash) value rather than amortised cost to reflect commitment at maturity.



f) The Treasury Management Code of Practice requires the maturity of borrowing to be determined by reference to the earliest date on which the lender can require payment. The Council's three LOBO loans are therefore presented as maturing in 2012-13, due to the six monthly break clauses, whereby the lender can opt to increase the rate, and the Council can choose to accept or decline the new rate. However it is not anticipated that the lender will opt to increase the rates at the break dates in the current interest rate environment.

g) The final maturity date on two of the Council's LOBO loans, totalling £15.6m, falls in 2014-15. Options for the repayment and, if applicable, refinancing of these loans will be fully considered and evaluated as their maturity date approaches, and advice taken from Sector, the Council's treasury management advisors.

3.2.8 Short Term Borrowing

a) The year-end position on temporary borrowing, and the range of rates applied, is set out below.

Short Term Debt Outstanding at 31st March 2012	Principal	Proportion of Debt	Range of Interest Rates	
			From	To
	£000	%	%	
Northampton Volunteering Centre	239	49	0.41	0.46
Billing Parish Council	90	42	0.41	0.46
HCA Principal due within 1 year	19	9	9.25	9.25
Total	**348**	**100**		

b) The Council has long-standing agreements with two local organisations, Billing Parish Council and Northampton Volunteering Centre, for the short-term deposit of funds with the Council. Accounting regulations require that these be treated in the accounts as short-term borrowing. The interest rate applicable on these accounts is set quarterly using the Council's average investment rate for the previous quarter, less 0.5% to cover administrative costs.

c) The repayment of the principal element of the HCA annuity (£19k) due in 2012-13 is also treated as short term borrowing in the accounts in accordance with accounting requirements.

Performance Report - Investments

3.2.9 Investments Strategy

a) The CLG Guidance on Local Government Investments requires Councils to set an Investment Strategy. This should set out the authority's policies for the prudent management of its investments and for giving priority, firstly to the security of those investments and secondly, to their liquidity. It should therefore identify the procedures for monitoring, assessing and mitigating the risk of loss of invested sums and for ensuring that such sums are readily accessible for expenditure whenever needed. The Council's Investment Strategy for 2011-12 was included in the Treasury Strategy for 2011-12, approved by Council at its meeting on 28 February 2011.

b) The CLG Guidance on Local Government Investments requires that investments are split into two categories:

(i) Specified investments – broadly, sterling investments, not exceeding 364 days and with a body or investment scheme of high credit quality.

(ii) Non-specified investments – do not satisfy the conditions for specified investments. This may include investment products that would normally be considered as specified investments, but are judged to have a higher level of risk than normal attached to them.

c) The Council's Investment Strategy for 2011-12 set out the Council's credit rating criteria for specified investments, including its definition for high credit quality, and the types of unspecified investments that it might enter into, including investments over 364 days.

d) The Council defines high credit quality in terms of investment counterparties as those organisations that:

- Meet the requirements of the creditworthiness service provided by the Council's external treasury advisers for defined periods of investment, and,
- Have sovereign ratings of AAA, and/or are
- UK nationalised or part nationalised banking institutions, or are
- UK banks or building societies supported by the UK banking system support package or are
- UK national or local government bodies or are
- Triple A rated Money Market funds

e) Investments periods are determined in line with the maximum periods recommended by Sector, the Council's treasury management advisor. In addition, the Investment Strategy imposes Council specific value and investment period limits for each category of approved counterparty.

f) The maximum limits in 2011-12 for placements with individual or group counterparties were £15m and 729 days for UK nationalised or part nationalised banking institutions and UK banks or building societies supported by the UK banking system support package, and £12m and 729 days for counterparties having sovereign ratings of AAA (Overseas or UK). Within this framework lower limits applied depending on credit ratings and other factors specific to each institution.

g) Instant access deposit accounts and call accounts continued to be used during 2011-12 to ensure liquidity and security of funds. The average balance in deposit and call accounts throughout the year was £2.6m.

h) The Council also makes use of triple-A rated money market funds. These have the benefits of high credit rating, high liquidity, easy access to funds, portfolio diversification, competitive returns, and administrative convenience. The average balance in money market funds throughout the year was £9.9m.

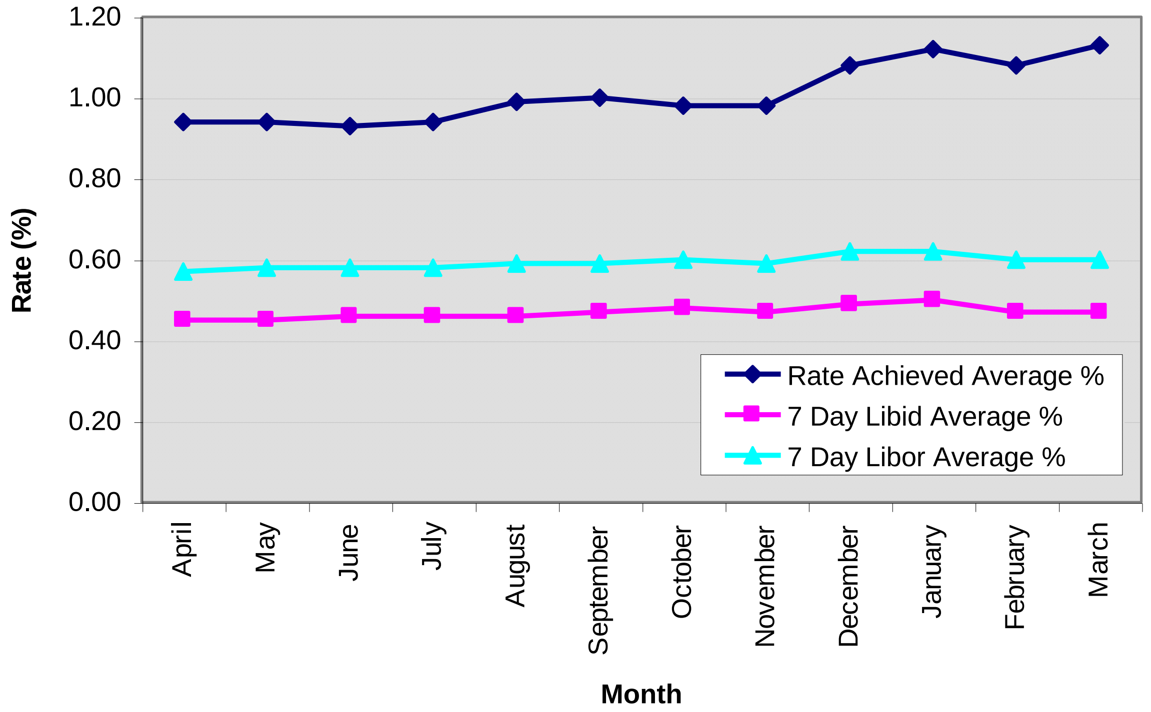
i) Most investments were held for cashflow purposes. Thirty-nine fixed term money market investments were made during the year. The range of investment periods was from 7 days to 364 days. No investments over 364 days were placed during the year. The average investment period was 119 days.

j) The total value of investments held at 31 March 2012, at amortised cost for money market investments over three months and cash values all other investments, was £37.1m. All investments were placed with reference to the pre-determined lending list, in line with the investment strategy. The breakdown of investments at year-end is shown in the table below:

Investment Type	**Balance at 31 March 2012**	
	£m	%
Cash & Cash Equivalents		
Deposit accounts	0.1	0.3
Call Accounts	10.0	27.0
Money Market Funds	3.9	10.5
Fixed Term Investments	11.0	29.6
Short Term Investments under 1 year		
Short Term Investments – Fixed Term	12.1	32.6
Total	**37.1**	**100.0**

k) The graph below shows the analysis of the Council's performance on investment returns during 2011-12 by plotting the Council's average monthly investment rate achieved against the average 7 day London Interbank Bid Rate (LIBID), and the average 7 day London Interbank Offered Rate (LIBOR).

Average Temporary Investment Rate Acheived Against 7 Day LIBID and LIBOR Rates



l) The Council's rate of return was stable during the first half of the year between 0.4% and 0.5% over LIBID. Performance improved during the second half of the year due to investments that were entered into at more favourable interest rates thus enabling the Council to achieve a higher variance above the LIBID rate. The average rate achieved was 1%. This was above the target rate of LIBID (0.47%), and of LIBOR (0.59%). The differential to LIBID represents a value of £5,300 per £1m invested per annum.

m) The Council does not hold any financial instruments listed or publicly traded on a stock exchange.

Performance Report - Debt Financing Budget Outturn

3.2.10 **Appendix B** shows the budget, outturn and variance for the Council's General Fund debt and investment portfolio in 2011-12. This demonstrates the revenue (current) effects of the treasury transactions executed. A summary is set out below:

Budget Comparison	**Approved Budget 2011-12 £000**	**Outturn 2011-12 £000**	**Variance 2011-12 £000**
Debt Financing & Interest	1,899	1,411	(488)

The most significant components of the outturn variance are as follows:

- £324k saving on Minimum Revenue Provision (MRP) due to carry forwards from the 2010-11 capital programme, and the optimisation of capital expenditure financing in 2010-11 through using capital receipts rather than borrowing

- £223k additional interest earned on investments (net of recharges for HRA cash balances) due to levels of cash balances and interest rates achieved being higher than budgeted

Prudential Indicators and Treasury Management Indicators

3.2.11 Throughout the course of the year, the Council's treasury staff have monitored the prudential Indicators and the treasury management indicators set for 2011-12. The outturn indicators are shown at **Appendix C.** Figures are shown at original (cash) value rather than amortised cost, in line with the requirements of the Prudential Code. There have been no breaches of limits during the 2011-12 financial year.

Compliance with agreed policies and practices, and statutory and regulatory requirements

3.2.12 The Council's officers and members have individual and collective responsibilities to comply with agreed policies and practices and statutory and regulatory requirements. These are set out in detail in the Schedules to the Council's Treasury Management Practices (TMPs).

3.2.13 Compliance has been monitored during the year. An investment of £5m made with Clydesdale Bank on 17 October 2011 was rolled over for a further three months on 17 January 2012, after the bank had been removed from the Council's recommended counterparty list. The investment was returned to the Council, with interest, on the due date. Procedures have been tightened up to prevent a similar occurrence in the future.

Compliance with CIPFA Code Recommendations

3.2.14 Under the umbrella of compliance with regulatory requirements, the Council has sought to comply with the requirements of the CIPFA Treasury Management Code of Practice. No breaches have been recorded during the 2011-12 financial year.

4. Implications (including financial implications)

4.1 Resources and Risk

4.1.1 The resources required for the Council's debt management and debt financing budgets are agreed annually through the Council's budget setting process. The debt financing budget outturn position is shown at paragraph 3.2.10 and **Appendix B**.

4.1.2 The risk management of the treasury function is specifically covered in the Council's Treasury Management Practices (TMPs), which are reviewed annually. Treasury risk management forms an integral part of day-to-day treasury activities.

4.1.3 The risk implications of decisions taken and transactions executed during 2011-12 financial year are discussed in the body of the report at paragraph 3.2.6.

4.2 Legal

4.2.1 The Council is obliged to carry out its treasury management activities in line with statutory requirements and associated regulations and professional guidance. The relevant legislative and regulatory documents are referred to within the report and listed in the background papers.

4.3 Other Implications

Policy

4.2.1 The Council is required to adopt the latest CIPFA Treasury Management Code of Practice, and to set and agree the following policy and strategy documents:

a) A Treasury Management Policy Statement

b) Treasury Management Practices (TMPs) and TMP Schedules

c) An annual Treasury Strategy incorporating:

(i) The Capital Financing and Borrowing Strategy for the year including:

- The Council's policy on the making of Minimum Revenue Provision (MRP) for the repayment of debt, as required by the Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008.

- The Affordable Borrowing Limit for the year as required by the Local Government Act 2003.

(ii) The Investment Strategy for the year as required by the CLG revised Guidance on Local Government Investments issued in 2010.

d) A mid-year review report and an annual review report of the previous year.

With the exception of those at (d) above, these policy documents are reported to Cabinet and Council as part of the budget setting process. The Council's Treasury Strategy for 2011-12 was approved by Council at its meeting on 28 February 2011.

This report complies with the requirement at (d) to prepare and submit to Council an annual treasury management review report.

4.3.2 The updated CIPFA Treasury Management Code of Practice requires the Council to place emphasis on the scrutiny of treasury management strategies and policies. This includes the nomination of the body (such as an audit or scrutiny committee) responsible for ensuring effective scrutiny of the treasury management strategy, policies and practices. The Audit Committee has been nominated for this role, which includes the review of all treasury management policies and procedures, the review of all treasury management reports to Cabinet and Council, and for making recommendations to Council.

Equality

4.3.3 An Equalities Impact Assessment was carried out on the Council's Treasury Strategy for 2011-12, and the associated Treasury Management Practices (TMPs) and the Schedules to the TMPs. This was included as an annex to the report to Cabinet on 23 February 2011 and to Council on 28 February 2011.

4.3.4 As a result of that assessment, it was noted that the potential impact of the strategy and associated documents (including Treasury Management Practices (TMPs) and the Schedules to the TMPs) on the different equalities groups must be considered as it is developed and put together each year. This includes the consideration of the potential impact on the different equalities groups of any processes, procedures or outcomes arising from these.

Consultees (Internal and External)

4.3.5 Consultation on treasury management matters is undertaken as appropriate with the Council's treasury advisors, Sector, and with the Portfolio holder for Finance.

4.3.6 Under the regulatory requirements, the Audit Committee has been nominated by Council as the body responsible for ensuring effective scrutiny of the treasury management strategy, policies and practices. This role includes the review of all treasury management policies and procedures, the review of all treasury management reports to Cabinet and Council, and the making of recommendations to Council. Audit Committee reviewed and noted the draft Treasury Management Outturn 2011-12 report and appendices at their meeting on 23 July 2012.

How the Proposals deliver Priority Outcomes

4.3.7 The Council has adopted the CIPFA Code of Practice on Treasury Management in the Public Services: Code of Practice and Cross Sectoral Guidance Notes ("the Treasury Management Code of Practice").

4.3.8 Under the umbrella of the Treasury Management Code of Practice, the Council's Treasury Management Policy Statement "…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 value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management."

4.3.9 This supports the Council's priority outcome of public money used to maximum benefit. (Priority 4 - making every £ go further).

5. Background Papers

5.1 Statute, Regulation and Guidance

- Local Government Act 2003
- Local Authorities (Capital Finance and Accounting) (England) Regulations 2003
- ODPM Guidance on Local Government Investments 2004
- CIPFA Prudential Code for Capital Finance in Local Authorities – Fully Revised Guidance Notes for Practitioners 2007
- The Local Authorities (Capital Finance & Accounting) (Amendments) (England) Regulations 2008
- CIPFA Treasury Management in the Public Services - Code of Practice and Cross-Sectoral Guidance Notes (Fully Revised Second Edition) 2009
- CIPFA Prudential Code for Capital Finance in Local Authorities (Fully Revised Second Edition) 2009
- CIPFA Treasury Management in the Public Services - Guidance Notes for Local Authorities including Police Authorities and Fire Authorities (Fully Revised Third Edition) 2009
- Local Authorities (Capital Finance and Accounting) (Amendment) (England) Regulations 2010
- CLG Guidance on Local Government Investments (2010)
- CIPFA Code of Practice on Local Authority Accounting in the United Kingdom 2010-11

- CLG Guidance on Minimum Revenue Provision (2010)

- Localism Act 2011

5.2 Reports to Cabinet & Council

- Treasury Strategy 2011-12 to 2013-14 – Report to Cabinet 23 February 2011 & Council 28 February 2011

- Prudential indicators for Capital Finance 2011-12 to 2013-14 - Report to Cabinet 23 February 2011 & Council 28 February 2011

- Treasury Management Mid Year Report 2011-12 – Report to Cabinet 23 November 2011 & Council 16 January 2012

5.3 Reports to Audit Committee

- Treasury Management Outturn 2011-12 – Report to Audit Committee 23 July 2012

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