FULL COUNCIL

8 FEBRUARY 2017

REPORT OF THE HEAD OF CENTRAL SERVICES

PRUDENTIAL INDICATORS AND TREASURY MANAGEMENT STRATEGY

1.0 PURPOSE OF REPORT

1.1 This report outlines the Council's prudential indicators for 2017/18 – 2019/20 and sets out the expected treasury operations for this period. It fulfils four key legislative requirements:

(a) The reporting of the **prudential indicators** setting out the expected capital activities (as required by the CIPFA Prudential Code for Capital Finance in Local Authorities). The treasury management prudential indicators are now included as treasury indicators in the CIPFA Treasury Management Code of Practice and Guidance Notes 2011 as revised.

(b) The Council's **Minimum Revenue Provision (MRP) Policy**, which sets out how the Council will pay for capital assets through revenue each year (as required by Regulation under the Local Government and Public Involvement in Health Act 2007);

(c) The **treasury management strategy statement** which sets out how the Council's treasury management service will support the capital decisions taken, the day to day treasury management activity and the limitations on activity through treasury prudential indicators. The key indicator is the **Authorised Limit**, the maximum amount of debt the Council could afford in the short term, but which would not be sustainable in the longer term. This is the Affordable Borrowing Limit required by s3 of the Local Government Act 2003. This is in accordance with the CIPFA Code of Practice on Treasury Management and the CIPFA Prudential Code ;

(d) The **investment strategy** which sets out the Council's criteria for choosing investment counterparties and limiting exposure to the risk of loss. This strategy is in accordance with the Department of Communities and Local Government (CLG) Investment Guidance.

The above policies and parameters provide an approved framework within which the officers undertake the day to day capital and treasury activities.

2.0 RECOMMENDATIONS

The Budget and Strategic Planning Working Group recommends to the Council that:

2.1 The prudential indicators and limits are adopted and approved;

2.2 The Treasury Management Strategy and treasury management prudential indicators are adopted and approved;

2.3 The Minimum Revenue Provision (MRP) Statement which sets out the Council's policy on MRP is approved;

2.4 Group limits for term deposits with counterparties within the same banking group be increased to £9m (para 3.1.6 refers); and

2.5 The Revenues Business Partner be authorised to be added as a signatory for banking activities (para 3.3.3 refers)

3.0 **KEY ISSUES**

3.1 **Background**

3.1.1 One of the main changes in the CLG guidance is that there is greater member scrutiny of the treasury management policies. The Budget and Strategic Planning Working Group is the responsible body for scrutinising the Treasury Management Strategy as agreed by Full Council on 3 February 2011.The Budget & Strategic Planning Working Group scrutinised the strategy on 18th January 2017 and now recommends the report to Full Council for approval.

3.1.2 To facilitate the decision making process and support capital investment decisions the Prudential Code requires the Council to agree and monitor a minimum number of prudential indicators and for housing authorities these are separated for the HRA and non-HRA capital investment. The indicators are mandatory, but can be supplemented with local indicators if this aids interpretation and may cover three years ahead.

3.1.3 The indicators cover affordability, prudence, capital expenditure, external debt and treasury management and form the basis of in year monitoring through the Members' Newsletter. For the General Fund the indicators have also been split into General and Special Expenses (Melton Mowbray).

3.1.4 The indicators are purely for internal use by the Council and are not to be used as comparators between Councils, as any comparisons will be meaningless. In addition, the indicators should not be considered individually in that the benefit from monitoring will arise from the movement in the Council's indicators over time and the year on year changes.

3.1.5 In order to increase the return on investment the duration limit for fixed rate investments was amended as part of the mid year review and property funds added to the list of available investment instruments. This will allow deals to be placed more easily and increase the investment return whilst not placing the Council in any greater financial risk.

3.1.6 It is proposed that the group limits for counterparties within the same banking group be increased from £6m to £9m. This allows investments to be placed in the highest rated organisations and not reduce credit criteria to ensure sufficient allowance when investment levels are at their highest. The current limits of £6m for individual counterparties and £6m group limits does not offer enough flexibility to achieve the highest investment return without increasing the financial risk.

3.2 **Treasury Management Strategy and Prudential Indicators**

3.2.1 The prudential indicators have been based on the position set out in the capital programme and revenue budget reports set out elsewhere on this agenda and the draft Medium Term Financial Strategy (MTFS). Along with each indicator is an explanation of what it demonstrates.

3.2.2 The Treasury Management Strategy is attached as Appendix A including the prudential indicators that relate to the treasury management function. This strategy covers the operation of the treasury function and its activities for the forthcoming year. The strategy has been informed by advice received from the Council's treasury management consultants.

3.2.3 The Council's treasury management consultants advise clients to adopt a creditworthiness service. This system uses a wide array of information, not just primary ratings, and by using a risk weighted scoring system, does not give undue reliance on just one agency's ratings. The weekly Capita Asset Services counterparty list is produced on this basis. Counterparties allocated a colour coding based on this criteria can be used. The durational limits suggested by Capita Asset Services have now been superseded by the recommendation in the mid year review as presented to this committee on 14 December 2016, counterparties with any colour coding can now be used for up to 12 months.

3.2.4 To summarise, the key issues set out in the attached appendix are as follows:

Capital Expenditure – The projected capital expenditure based on the available funding set out in the draft Medium Term Financial Strategy is estimated as set out in the following table:

Capital Expenditure	**2016/17 Revised £000's**	**2017/18 Estimated £000's**	**2018/19 Estimated £000's**	**2019/20 Estimated £000's**
General Expenses -CSA	531	588	237	237
General Expenses- PFA	158	27	0	59
General Expenses-REEA	5,394	231	159	51
Special Expenses-TAC	261	0	0	0
Total Non HRA	**6,394**	**1,196**	**396**	**347**
HRA	3,414	6,164	4,265	1,045
Total	**9,758**	**7,010**	**4,661**	**1,392**

Debt Requirement and Repayment – Part of the capital expenditure programme will be financed directly (through Government grants, capital receipts etc.), leaving a residue which will increase the Council's external borrowing requirement (its Capital Financing Requirement – CFR). The General Fund CFR is reduced each year by a statutory revenue charge for the repayment of debt known as the Minimum Revenue Provision or MRP (there is no requirement for an HRA charge). However, where unsupported borrowing is undertaken for the HRA it is considered prudent to do so. With regard to the self financing the Government stated that the repayment of borrowing is not required but the Council can opt to repay the debt rather than build up cash reserves where it considers this to be in the best interests of the Council and the Housing Service.

As illustrated earlier the Capital Finance and Accounting Regulations affecting MRP require the Council to formally approve a method for calculating MRP annually. From 1 April 2017 for all unsupported borrowing (including PFI and finance leases) the MRP policy will be:

Asset life method- MRP will be based on the estimated life of the assets, in accordance with the regulations (this option must be applied for any expenditure capitalised under a Capitalisation Direction) This option provides for a reduction in the borrowing need over approximately the asset's life. It is therefore recommended that the asset life method is used for unsupported borrowing as is the case for 2016-17.

Capital Financing Requirement - The following table sets out the predicted CFR for the period 2016-2020 analysed by fund, taking into account the method of calculating MRP as recommended above.

Capital Financing Requirement	**2016/17 Revised £000's**	**2017/18 Estimated £000's**	**2018/19 Estimated £000's**	**2019/20 Estimated £000's**
General Expenses	126	113	101	89
Total Non HRA	**126**	**113**	**101**	**89**
HRA	31,484	31,484	31,484	31,484
Total	**31,610**	**31,597**	**31,585**	**31,573**

The Council's anticipated net borrowing requirement (net of investments) is shown below with a comparison against the CFR. The Council needs to ensure that its total borrowing net of any investments, does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2016/17 and the next two financial years. This allows some flexibility for limited early borrowing for future years.

The Head of Central Services reports that the Council complied with this prudential indictor in the current year and does not envisage difficulties for the future. This view takes into account current commitments, existing plans and the assumptions set out in paragraph 3.2.1.

Net Borrowing	**2016/17 Revised £000’s**	**2017/18 Estimated £000’s**	**2018/19 Estimated £000’s**	**2019/20 Estimated £000’s**
Gross Borrowing	31,413	31,413	31,413	31,413
Investments	13,564	9,129	6,362	7,113
Net Borrowing	**17,849**	**22,284**	**25,051**	**24,300**
CFR	**31,622**	**31,610**	**31,585**	**31,573**

Against this borrowing need (the CFR), the Council's expected maximum external debt position for each year (the Operational Boundary), and the maximum amount it could borrow (the Authorised Limit) are set out as follows:

Authorised Limit & Operational Boundary	**2016/17 Revised £000’s**	**2017/18 Estimated £000’s**	**2018/19 Estimated £000’s**	**2019/20 Estimated £000’s**
Authorised limit	46,000	46,000	46,000	46,000
Operational boundary	36,539	36,526	36,514	36,502

The net revenue impact of the new capital schemes being approved as part of this budgetary cycle on Council Tax and housing rents are expected to be:

Incremental impact of capital investment decisions on:	**2016/17 Revised £**	**2017/18 Estimated £**	**2018/19 Estimated £**	**2019/20 Estimated £**
General Expenses Band D Council Tax	4.20	0.40	-2.17	1.59
Special Expenses Band D Council Tax	0	0	0	0
Housing rents levels	0	0	0	0

3.3 Operational Update

3.3.1 Members will be pleased to note that following a recent internal audit of Treasury Management function the audit team were able to provide a substantial level assurance that all processes and controls were operating affectively across all areas of the audit. In addition to this no issues or areas of improvement were identified. This reflects the operational effectiveness and due diligence of offers in their role as custodians of public funds for Melton.

3.3.2 Officers have also updated the Treasury Management Practices (TMPs) which set out the manner in which the Council will seek to achieve its treasury management policies and objectives and how it will manage and control those activities. These are operational practices which ensure roles, responsibilities and practices are clear and understood by officers. In line with good practice it is important these are kept up to date and reflect the current day to day operations.

3.3.3 In light of one of the Strategic Directors leaving it would be prudent for an additional signatory to be included for banking purposes. This will enable funds to be promptly invested and other banking activities, such as signing cheques having the required authorisation. It is recommended the Revenues Business Partner be added with immediate effect to the signatories.

4.0 POLICY AND CORPORATE IMPLICATIONS

4.1 There are no other major policy and corporate implications arising from this report.

5.0 **FINANCIAL AND OTHER RESOURCE IMPLICATIONS**

5.1 There are no other financial implications arising from this report.

6.0 **LEGAL IMPLICATIONS/POWERS**

6.1 There are no other legal implications arising from this report.

7.0 **COMMUNITY SAFETY**

7.1 There are no direct links to community safety arising from this report.

8.0 **EQUALITIES**

8.1 There are no direct equality issues arising from this report.

9.0 **RISKS**

9.1 The relevant risks are considered in the table on the following page:

Probability

Very High A				
High B				
Significant C				
Low D				
Very Low E			1,2	
Almost Impossible F				
	IV Neg-ligible	III Marg-inal	II Critical	I Catast-rophic

Impact

Risk No.	Description
1	Loss of Investment
2	Failure of counterparties

9.2 The relevant risks are considered to be of a very low probability, albeit of a critical nature and are mitigated by both investment and borrowing indicators/limits. In respect of borrowing there are upper limits for both fixed and variable interest rate exposure and limits for the Maturity Structure of Borrowing (see para 5.1.4 in Appendix A). These limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing.
The investment strategy (see Appendix A Section 4) contains limits covering maximum sums invested over 364 days, as well as benchmarks relating to the maximum security risk.

9.3 The use of a sophisticated modelling approach in selecting both counterparties and time periods utilising ratings from all three main rating agencies and supplemented with credit watches, credit outlooks, Credit Default Swaps (CDS) spreads and sovereign ratings will ensure only the most creditworthy institutions/countries are used.

10.0 **CLIMATE CHANGE**

10.1 There are no climate change issues arising from this report.

11.0 **CONSULTATION**

11.1 The Council's treasury management consultants have been consulted on this report.

12.0 **WARDS AFFECTED**

12.1 All wards are affected.

Contact Officer: Date:	Dawn Garton, Head of Central Services 23 January 2017
Appendices:	Appendix A - Treasury Management Strategy Statement Appendix B- Borrowing Indicators
Background Papers:	Prudential Indicators Working Papers MTFS Revenue Estimates Capital Programme
Reference:	X: C'tees, Council & Sub-C'tees/Full Council/2016-17/08-02-17/DG- Prudential Indicators and Treasury Management Strategy