Report to the Audit & Governance Committee

Report reference: AGC-006-2016/17
Date of meeting: 19 September 2016

Epping Forest District Council

Portfolio: **Finance**

Subject: **Annual Outturn Report on the Treasury Management and Prudential Indicators for 2015/16.**

Responsible Officer: **Simon Alford** **(01992 564455).**

Democratic Services Officer: **Gary Woodhall** **(01992 564470).**

Recommendations/Decisions Required:

(1) To consider how the risks associated with Treasury Management have been dealt with during 2015/16;

(2) To consider the proposed minor changes to the Council's Treasury Management Strategy Statement and Investment Strategy; and

(3) To make any comments or suggestions that Members feel necessary to the Cabinet.

Executive Summary:

The annual treasury management outturn report is a requirement of the Council's reporting procedures. It covers the treasury activity for 2015/16 and confirms that there were no breaches of policy during the year.

The risks associated with the treasury function are highlighted within the report along with how these risks were managed during the year.

In constructing the Treasury Management Strategy Statement and Investment Strategy for 2016/17 to 2018/19 some very prudent restrictions were applied to some classes of investments. It has become evident that these restrictions are too prudent and cause operational difficulty in managing the Council's cash flow. Some minor changes are proposed that will ease the operational difficulties without adding significantly to the risk profile of the Council's investments.

This report and the appendices will be considered by the Finance and Performance Management Cabinet Committee on 15 September and an oral update will be provided.

Reasons for Proposed Decision:

The proposed decision is necessary in order to show that the risks associated with the treasury strategy were managed during the year and to comply with the requirements of the CIPFA Code of Practice on Treasury Management on reporting on the performance of the treasury activity.

Other Options for Action:

Members could ask for additional information about the CIPFA Codes or the Prudential Indicators.

Members could propose that either no amendments to the Treasury Management Strategy Statement and Investment Strategy are appropriate or that amendments different to those recommended should be made.

Report:

Introduction

1. The Council's treasury activities are strictly regulated by statutory requirements and a professional code of practice (the CIPFA Code of Practice on Treasury Management), which includes the requirement for reporting on the treasury outturn on the financing and investment activity for the previous year.

2. The report attached at appendix 1 shows the Treasury Management Outturn Report for 2015/16 in accordance with the revised CIPFA Treasury Management Code and the revised Prudential Code.

Capital Activity in the Year

3. The Council undertakes capital expenditure on long-term assets. These activities may either be financed immediately through capital receipts, grants etc; or through borrowing.

4. The Council had planned to borrow to finance its capital investments, although as spending was lower than anticipated no borrowing was necessary. The capital programme outturn is shown below in the table:

Capital Expenditure	**2015/16 Original £m**	**2015/16 Revised £m**	**2015/16 Actual £m**
Non-HRA capital expenditure	7.476	32.012	23.488
HRA capital expenditure	18.952	17.905	13.811
Total Capital expenditure	**26.428**	**49.917**	**37.299**
Financed by:			
Capital grants	1.395	3.393	3.725
Capital receipts	8.002	16.373	19.046
Revenue	17.031	17.597	14.528
Borrowing	0	12.554	0
Total resources Applied	**26.428**	**49.917**	**37.299**
Closing balance on:			
Capital Receipts	4.662	7.523	3.788
Major Repairs Reserve	5.683	9.523	12.291

5. The closing balance on capital receipts is after taking into account new receipts being generated from the right to buy sales and for major repairs reserve the major repairs allowance received in the year.

6. The financial risk involved within the Capital Activity is the impact on reducing the

balance of usable capital receipts over the next three years. This risk has the following potential consequences; loss of interest; loss of cover for contingencies; service reductions required; and large Council Tax increases required.

7. The table above shows that the combined balances on Capital Receipts and Major Repairs Reserve are lower than expected. However, the anticipated borrowing of £12.6 million did not take place. Overall this means that moving forward the Council is in a similar position to that estimated and therefore it can be concluded that adequate resources still exist for the Capital Programme in the medium term.

The impact on the Council's indebtedness for capital purposes

8. The Council's underlying need to borrow is called the Capital Financing Requirement (CFR). This figure is a gauge for the Council's debt position. The Council has borrowed £185.456m to finance the payment to Government for Housing Self-Financing. This resulted in the Council CFR becoming an overall positive CFR (HRA and Non-HRA). No further borrowing was incurred in 2015/16.

CFR	**Original 31-Mar-16 £m**	**Revised 31-Mar-16 £m**	**Actual 31-Mar-16 £m**
Non-HRA	59.6	43.5	29.6
HRA	155.1	155.1	155.1
Closing balance	**214.7**	**198.6**	**184.7**

9. The Council did not breach the Authorised Limit (set at £230m for 2015/16) or the Operational Boundary (set at £219m for 2015/16) and the Maturity Structure of Fixed Rate Borrowing (restricted to 30 years and below).

10. The risks for Councils are associated with affordability, interest rates and refinancing – the affordability risk is whether the Council can afford to service the loan, this was achieved through the Council producing a viable thirty-year financial plan. This plan continues to be reviewed quarterly by officers and half yearly reports are presented to the Housing Scrutiny Panel. The interest rate risk is whether a change in interest rate could have an impact on the viability of the financial plan. Only 17% of the amount borrowed in 2011/12 was at a variable rate, the remainder were fixed at preferential rates. Any upward movement in interest rates would be 'hedged' by a corresponding increase in interest earned on Council investments. The refinancing risk is that maturing borrowings, capital project or partnership financing cannot be refinanced on suitable terms. Within the financial plan it is anticipated that all borrowing will be repaid on maturity and any borrowing to support future capital expenditure can easily be obtained from other local authorities or the PWLB.

The Council's treasury position

11. The table below shows the Council's level of balances for 2015/16.

Treasury position	**Original 31-Mar-2016 £m**	**Revised 31-Mar-16 £m**	**Actual 31-Mar-16 £m**
Usable Reserves	45.8	45.0	46.9
Working Capital	15.0	45.0	46.0

12. It is important that the cash flow of the Council is carefully monitored and controlled to

ensure enough funds are available each day to cover its outgoings. This will become more difficult as the Council uses up capital receipts and reduces investment balances.

13. The Council did not breach any of the following indicators:

a) The Maximum Upper Limit for Fixed Rate Exposure during 2015/16 was 83% for Debt and 71% for Investments (limit set at 100%) and Maximum Upper Limit for Variable Rate Exposure during 2015/16 was 17% on Debt and 29% on Investments (limit set at 25% and 75% respectively);

b) The maximum amount of the portfolio being invested for longer than 364 days was £0m (limit set at £30m); and

c) The maximum limit for investment exposure outside of the UK was set at 30%. The outturn was comfortably inside this at 12%, comprising an average £1m in Sweden, 2% and Standard Life MMF is domiciled in Guernsey so is also Non-UK with an average £5m, 10%.

14. The risks associated with this section are as follows:

a) Credit and Counterparty Risk – the risk of failure by a third party to meet its contractual obligations to the Council, i.e. goes into liquidation. The Council's counter-party lists and limits reflect a prudent attitude towards organisations with which funds may be deposited and these are regularly updated by our treasury advisors.

b) Liquidity Risk – the risk that cash will not be available when it is needed, incurring additional unbudgeted costs for short-term loans. The Director of Resources has monthly meetings with treasury staff, to go through the cash flow for the coming month. A number of instant access accounts are used to ensure adequate cash remains available.

c) Interest Rate Risk – the risk of fluctuations in interest rates. The Council allows a maximum of 75% of its investments to be invested in variable rates, and the remainder are in fixed rate deposits. This allows the Council to receive reasonable rates, whilst at the same time, gives the Council flexibility to take advantage of any changes in interest rates.

15. The prudential indicators within this section assist the Council to reduce the risk of:

a) Counterparties going into liquidation by ensuring only highly rated institutions are used when investing the Council's money.

b) The Council incurring unbudgeted short-term loans, to pay unexpected expenditure items through ensuring adequate level of money is available immediately through instant access accounts.

c) Potentially losing out on investment income when interest rates start to increase by ensuring that the majority of deposits are kept within one year.

Changes to the Current Treasury Management Strategy Statement and Investment Strategy

16. Since the approval of the Strategy by Council on 18 February 2016 it has become apparent that three of the limits within the Strategy are excessively prudent and obstruct the efficient management of the Council's cash flow. Therefore the following changes are

proposed -

Local Authorities as a group limit – increase from £20m to £25m.
Money Market Funds as a group limit – increase from £15m to £20m.
NatWest (the Council's banker) – increase from £2.5m to £5m.

17. The Council's treasury advisers, Arlingclose, have been consulted on the proposals and have confirmed that they are acceptable as long as money is only left with NatWest overnight.

18. Any change to the Strategy requires approval from Council so Members are invited to make comments on the recommended changes to the Cabinet so they can consider them before the proposals progress to Council.

Summary

19. The Council has continued to finance its capital programme through using internal resources. Combined balances on Capital Receipts and Major Repairs Reserve at the year-end were broadly similar to the anticipated closing balances, meaning the Council still has adequate resources going forward to finance its medium term capital programme. The Council procured no new borrowing and did not breach any of the treasury prudential indicators during the year.

Resource Implications:

As outlined within the report.

Legal and Governance Implications:

The Council's treasury management activities are regulated by a variety of professional codes, statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken (although no restrictions were made in 2009/10 or subsequently);
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
- Under the Act the ODPM (now DCLG) has issued Investment Guidance to structure and regulate the Council's investment activities.
- Under section 21(1) AB of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices. Guidance on Minimum Revenue Provision was issued under this section on 8 November

2007.

Safer, Cleaner and Greener Implications:

None.

Consultation Undertaken:

The Council's external treasury advisors provided the framework for this report and have confirmed that the content satisfies all regulatory requirements.

Background Papers:

The report on the Council's Prudential Indicators for 2015/16 and the Treasury Management Strategy for 2015/16 to 2016/17 went to Council on 17 February 2015.

Risk Management:

As detailed in the report, a risk aware position is adopted to minimise the chance of any loss of the capital invested by the Council. The specific risks associated with the different aspects of the treasury management function have been outlined within the main report.

Due Regard Record

This page shows **which groups of people are affected** by the subject of this report. It sets out **how they are affected** and how any **unlawful discrimination** they experience can be eliminated. It also includes information about how **access to the service(s)** subject to this report can be improved for the different groups of people; and how they can be assisted to **understand each other better** as a result of the subject of this report.

S149 Equality Act 2010 requires that due regard must be paid to this information when considering the subject of this report.

No groups of people are affected by this report which is not directly service related.