

**Report of Chief Officer Financial Services**

**Report to Corporate Governance and Audit Committee**

**Date: 16<sup>th</sup> March 2020**

**Subject: Annual Treasury Management Governance Report**

Are specific electoral Wards affected? If relevant, name(s) of Ward(s):	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Has consultation been carried out	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Are there implications for equality and diversity and cohesion and integration?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Is the decision eligible for Call-In?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Does the report contain confidential or exempt information? If relevant, Access to Information Procedure Rule number: Appendix number:	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

**Summary**

**1. Main issues**

1. This annual report provides assurance that the Treasury Management (TM) function is operating within its governance framework.
2. TM fully complies with the current CIPFA Code of Practice, the Prudential Code and the revised guidance notes for practitioners issued in 2017.
3. Since the last update all borrowings and investments undertaken have been in accordance with the approved governance framework.
4. TM operates within the governance framework and also uses additional market intelligence and information gathered from a variety of sources. These sources have been integral to protecting the authority from undue risk in the financial and money markets.
5. Internal Audit has provided substantial assurance on the control environment and compliance in their 2018/19 audit report.

## **2. Best Council Plan Implications**

- 2.1 Treasury Management strategy secures funding to support the Council's Policies and City Priorities as set out in the Council capital programme and is consistent with the Best Council Plan.

## **3. Resource Implications**

- 3.1 This treasury strategy recognises the borrowing necessary to fund the capital programme requirements of both General Fund and HRA. The revenue costs of borrowing are included within the revenue budgets of the general fund and HRA.

## **Recommendations**

1. Note that Treasury Management continues to adhere to its governance framework including the CIPFA Code of Practice, the Prudential Codes 2017 and revised CIPFA guidance notes issued in 2018. All borrowing and investments undertaken have been compliant with the governance framework.

## **1 Purpose of this report**

- 1.1 This annual report outlines the governance framework for the management of the Council's TM function

## **2 Background information**

- 2.1 The operation of the TM function is governed by provisions set out under part 1 of the Local Government Act 2003 whereby the Council is required to have regard to the Chartered Institute of Public Finance and Accountancy (CIPFA) Prudential Code for Capital Finance in Local Authorities 2017 in particular: The Prudential Code requires that full Council set certain limits on the level and type of borrowing before the start of the financial year together with a number of Prudential indicators.
- Any in year revision of these limits must be set by Council.
  - Policy statements are prepared for approval by the Council at least two times a year.
- 2.2 TM is responsible for managing the Housing Revenue Account and General Fund external debt which is in the region of £2,239m and investments that currently stand at around £45m. It also manages the cash flow requirements of the Council.

## **3 Main issues**

- 3.1 The role of the Corporate Governance and Audit Committee is to ensure that TM is adhering to and operating within its governance framework, as shown in Appendix A.
- 3.2 During the year TM had continued to comply with the Chartered Institute of Public Finance and Accountancy (CIPFA) Code of Practice on Treasury Management, Prudential Code (2017) and its guidance notes (2018). As such a strategy report was presented to Executive Board in February 2018 together with an update in November 2018. A further outturn report for the previous financial year was presented in June 2019. For the Year 2019/20 a strategy report was presented to Executive Board in February 2019 together with an update in November 2019.
- 3.3 During the year all borrowings and investments undertaken have been in accordance with the approved governance framework and are in line with the Treasury Management Policies and Practices.
- 3.4 In recent years the treasury strategy has taken advantage of the low short-term interest rates to fund its long term borrowing requirement. The Councils balance sheet strength has also been used to defray long term borrowing and avoid the risk associated with external Treasury Management investments.
- 3.5 The 2020 February Executive Board update report has highlighted that the borrowing strategy has been updated during 2019/20 with the emphasis now on locking out risk in the Treasury management debt budget by taking longer term loans at historic low rates to fund the borrowing requirement of the capital programme and from internal cash balances. In November 2017 the Monetary Policy Committee (MPC) increased the bank rate for the first time in 8 years reversing the last cut made in August 2016. A further increase of 0.25% to 0.75% was made in August 2018 and have remained at this level since. Further increases

are expected going forward but expectations are that these increases will be introduced slowly and steadily. Pending locking out risk by taking longer term funding, the amount of debt that the Council is funding from short term loans and its balance sheet is forecast to fall to £390m by 31/03/2020. This exposure is considered manageable given historical capital programme slippage, the strength of the Council's balance sheet and the market for supplying short term funds remaining strong. These factors will continue to be monitored and should be considered in the context of the stability of the current debt maturity profile.

- 3.6 The Council's current long term debt of £2,098m has an average maturity of just under 38 years if all debts run to maturity. Approximately 11% of the Council's long term fixed debt has options for repayment which are the LOBO's excluding Barclays loans which are now fixed. In the unlikely event that all these options were exercised at the next option date then the average maturity of long term debt would be lowered to just under 33 years. This compares favourably with the average maturity of the UK's government gross debt portfolio of 15.35 years. The existing profile of the Council's debt provides considerable certainty of funding costs with 82% or £1,668m of its total debt maturing in periods greater than 10 years.
- 3.7 The Lenders Option Borrowers Option loans (LOBO's) that many Local Authorities issued up to 2007/08 have been used successfully over the last 20 years to reduce the Councils interest costs in comparison to Public Works Loan Board (PWLB) funding available at the time. These loans also introduced short to medium term re-financing risk at a time when the average maturity of the Councils debt portfolio was becoming very long. In essence the standard LOBO's that the Council has issued are long dated loans, which after an initial fixed period, contain an option whereby the lender only can vary the rate of interest on the loan, but only at specific intervals. These periods are every 3, 5 or 6 years depending on the specific loan. If the lender exercises the option the Council then has the option to accept the change or to repay the loan without any penalty cost and repay the principal in full. No options have been exercised since 2008 and in the current economic climate these loans are essentially fixed.
- 3.8 The Council has £215m of LOBO loans with Barclays of which £110m are the subject of a class action initiated by a total of 7 Councils. These LOBOs contained clauses that referenced London Inter Bank Overnight Rate (LIBOR) at a time when Barclays were subsequently convicted and fined for fraudulently fixing LIBOR. This is an ongoing action and further details will be reported as appropriate as the action progresses.
- 3.9 The Council's total external borrowing Capital Financing Requirement CFR i.e. the amount required to fund previous and current capital expenditure is circa £2,354m and its assets are valued at £5,671m as at 31 March 2019. The setting and monitoring of the capital programme seeks to ensure that we invest and maintain our assets whilst supporting the best council plan priorities. Treasury Management strategy determines the revenue affordability of the programme.
- 3.10 To mitigate against the exposure to rising interest rates the Council continues to explore forward funding options which will give the Council the ability to lock in future funding at near current rates.
- 3.11 TM continues to review key aspects of the framework including prudential indicators to ensure that they continue to be fit for purpose and provide the right evidence that TM is operating within acceptable levels of risk. The strategy updates to Executive Board include an update on prudential indicators. TM is complying with all of

CIPFA's prudential indicators as shown at Appendix B which was reported to Executive Board on 12<sup>th</sup> February 2020.

- 3.12 The operation of TM within its governance framework is also complemented by additional market intelligence and information gathered from a variety of sources. These tools involve:
- The use of real time market information on the financial and money markets in the UK, Europe, US and other major economies;
  - Discussions with market participants and brokers;
  - Use of treasury advisors to test market views;
  - Networking and sharing of information with Core Cities and West Yorkshire districts;
  - Attending market seminars providing technical and economic updates;
  - Daily market updates from financial institutions and brokers;
  - Thorough review of new financial products and how they fit within the governance structure; and
  - Undertaking continuing professional development and ensuring that appropriate training is undertaken.
- 3.13 Furthermore TM undertakes to respond to all treasury management consultations and influence the national governance framework, through attendance at regular core city meetings.
- 3.14 Internal Audit has completed its annual review of the TM function for the year 2018/19 which is the most recent audit review. This involved a risk based system audit of TM to evaluate and validate key systems controls.

### **Treasury Management & Bankline 2018/19**

Key controls for a sample of investments, loans and interest payments for 2018/19 were reviewed. The Internal Audit report issued 21<sup>st</sup> June 2019 provided the highest level of assurance for the control environment and compliance with the control environment.

## **4 Corporate Considerations**

### **4.1 Consultation and Engagement**

4.1.1 There has been no consultation in relation to this report

### **4.2 Equality and Diversity / Cohesion and Integration**

4.2.1 This report does not have any direct equality and diversity/cohesion and integration issues.

### **4.3 Council policies and Best Council Plan**

4.3.1 The execution of the Treasury Management strategy secures funding to support the Council's Policies and City Priorities as set out in the Council capital programme and is consistent with the Best Council Plan.

## **Climate Emergency**

- 4.3.2 The Council declared a Climate Emergency at full Council in March 2019. As the Treasury Management strategy secures funding for the Council's capital programme the impact of the Council's activity and implications for the climate emergency will be considered in each individual capital programme and scheme project report.

### **4.4 Resources, procurement and value for money**

- 4.4.1 The execution of the Treasury Strategy enables funds to be raised and managed in the most efficient manner in line with the approved strategy as presented to Executive Board on 14<sup>th</sup> February 2019 and 12<sup>th</sup> February 2020.

### **4.5 Legal Implications, Access to Information and Call In**

- 4.5.1 The legislative framework which governs TM is outlined in section 2.1. This framework includes compliance with the CIPFA Treasury Management Code of Practice, the prudential code 2017 and revised guidance notes issued in 2018 as revised.

- 4.5.2 There are no legal or access to information issues arising from this report.

### **4.6 Risk Management**

- 4.6.1 As set out in the Treasury Management Policy Statement, TM activities are carried out within a risk management framework and the management of risk is key to securing and managing the Council's borrowing, lending and cash flow activities.
- 4.6.2 By complying with and adopting the CIPFA Treasury Management Code of Practice, Prudential Code and guidance notes, assurance is given that arrangements are in place to manage risks effectively.

## **5 Conclusions**

- 5.1 This report confirms that the treasury management governance framework is up to date and fit for purpose, that the Council is operating within its governance framework and as such is complying with the CIPFA Treasury Management Code of Practice, Prudential Code and updated guidance notes. A 2018/19 Internal Audit report gave TM substantial assurance on both control and compliance. It also confirms that the strategy is being monitored and reported back to Executive Board and full Council as appropriate.

## **6 Recommendations**

- 6.1 Note that Treasury Management continues to adhere to its governance framework including the CIPFA Code of Practice, the Prudential Codes 2017 and revised CIPFA guidance notes issued in 2018. All borrowing and investments undertaken have been compliant with the governance framework.

## **7 Background documents<sup>1</sup>**

- 7.1 None

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<sup>1</sup> The background documents listed in this section are available to download from the Council's website, unless they contain confidential or exempt information. The list of background documents does not include published works.

## Treasury Management Governance Framework

<b>FULL COUNCIL</b>	<b>EXECUTIVE BOARD</b>	<b>CORPORATE GOVERNANCE &amp; AUDIT COMMITTEE</b>	<b>RESOURCES AND COUNCIL SERVICES SCRUTINY BOARD</b>
Setting Borrowing limits	Treasury Management Strategy	Adequacy of Treasury Management policies and practices	Review / scrutinise any aspects of the Treasury management function
Changes to borrowing limits	Monitoring reports in year	Compliance with statutory guidance	
Treasury Management Policy	Performance of the treasury function		
<b>↓ DELEGATIONS TO OFFICERS</b>			
<b>DELEGATION SCHEME</b>	<b>TO WHOM</b>	<b>FUNCTION DELEGATED</b>	
Part 3 Section 3E(d) Officer Delegation Scheme	To Chief Officer Financial Services	to discharge the following functions 1) Ensuring effective financial management and controls, including:- b) managing the Council's borrowing and investment requirements;	
Miscellaneous Functions - Financial Regulation 23: Treasury Management Page 35	Function delegated to Chief Officer (Financial Services).  Delegated to Head of Finance – Technical.	To ensure that all investment and borrowing is valid, accurate, efficient, properly accounted for and in accordance with statutory and corporate requirements	

**↓ OPERATIONAL AUTHORITY OF OFFICERS/CONTROL FRAMEWORK**

<b>POLICY DOCUMENT</b>	<b>TO WHOM</b>	<b>OPERATIONAL AUTHORITY</b>
Treasury Management Policy Statement (section 11) Policy on Delegation and Review Requirements and Reporting Arrangements	Chief Off. Financial Services Head of Finance - Technical Senior Treasury Manager Assistant Finance Manager	Implementation of decisions taken at Treasury strategy review meetings and day to day management of treasury operations
CIPFA: Code of Practice Prudential Code MHCLG Investment Guidance Notes	Head of Finance - Technical Senior Treasury Manager Assistant Finance Manager	Ensure compliance and that any changes are reflected in the operating framework.

No.	PRUDENTIAL INDICATOR	2019/20	2020/21	2021/22	2022/23
<b>(1). EXTRACT FROM BUDGET AND RENT SETTING REPORTS</b>					
1a	<b>Ratio of Financing Costs to Net Revenue Stream</b>				
	General Fund (Borrowing Only)	12.35%	18.08%	20.43%	22.10%
1b	General Fund (Borrowing and Other Long Term Liabilities)	21.36%	27.13%	29.50%	30.74%
2a	HRA (Borrowing Only)	11.63%	11.52%	11.53%	11.78%
2b	HRA (Borrowing and Other Long Term Liabilities)	18.64%	18.19%	18.13%	18.27%
		£'000	£'000	£'000	£'000
5	<b>Gross external borrowing requirement (Gross Debt and CFR)</b>	2,239,000	2,414,000	2,598,000	2,753,000
	The Net Borrowing Requirement should not exceed the capital financing requirement (Note 3)	OK	OK	OK	OK
	<b>Estimate of total capital expenditure</b>	£'000	£'000	£'000	£'000
6	General Fund	290,386	434,209	289,556	172,978
7	HRA	97,680	154,067	155,671	143,018
	TOTAL	388,066	588,276	445,227	315,996
	<b>Capital Financing Requirement (as at 31 March)</b>	£'000	£'000	£'000	£'000
8	General Fund	2,242,013	2,353,759	2,467,790	2,562,618
9	HRA	810,753	851,819	896,676	930,512
	TOTAL	3,052,766	3,205,578	3,364,466	3,493,130

No.	PRUDENTIAL INDICATOR	2019/20	2020/21	2021/22	2022/23
<b>(2). TREASURY MANAGEMENT PRUDENTIAL INDICATORS</b>					
		£'000	£'000	£'000	£'000
10	<b>Authorised limit for external debt</b>				
	borrowing	2,600,000	2,800,000	3,000,000	3,150,000
	other long term liabilities	690,000	660,000	580,000	540,000
	TOTAL	3,290,000	3,460,000	3,580,000	3,690,000
11	<b>Operational boundary -</b>				
	borrowing	2,450,000	2,650,000	2,850,000	2,850,000
	other long term liabilities	670,000	640,000	560,000	520,000
	TOTAL	3,120,000	3,290,000	3,410,000	3,370,000
14	<b>Upper limit for fixed interest rate exposure (note 5)</b>				
	expressed as either:-				
	Net principal re fixed rate borrowing / investments OR:-	115%	115%	115%	115%
	Net interest re fixed rate borrowing / investments				
15	<b>Upper limit for variable rate exposure (note 5)</b>				
	expressed as either:-				
	Net principal re variable rate borrowing / investments OR:-	40%	40%	40%	40%
	Net interest re variable rate borrowing / investments				
		£'000	£'000	£'000	£'000
17	<b>Upper limit for total principal sums invested for over 364 days (Note 6)</b>	150,000	150,000	150,000	150,000
18	<b>Net Debt as a percentage of Gross debt</b>	98.66%	98.76%	98.85%	98.91%

16	Maturity structure of fixed rate borrowing 2019/20	Lower Limit	Upper Limit	Projected 31/03/2020	
	under 12 months	0%	15%	0%	
	12 months and within 24 months	0%	20%	3%	
	24 months and within 5 years	0%	35%	10%	
	5 years and within 10 years	0%	40%	5%	
	10 years and within 20 years			5%	
	20 years and within 30 years			0%	
	30 years and within 40 years	25%	90%	35%	82%
	40 years and within 50 years			35%	
	More Than 50 Years			6%	
				100%	

## Notes.

- The indicator for the ratio of financing costs to net revenue stream for General Fund is now calculated based on the External Borrowing costs only and Borrowing and Other long term Liabilities (PFI and leasing)
- The Changes to the Prudential Code 2017 retired the Indicator 3 and 4 on the incremental impact of New Capital decision on HRA and GF as well as Indicator 13 the need to explicitly adopt the Code of Practice. In addition Indicator 9 the relating to the MHCLG imposed HRA borrowing debt ceiling has been recinded and is therefore no longer reported
- In order to ensure that over the medium term gross borrowing will only be for a capital purpose, the Council should ensure that gross external borrowing does not exceed the total capital financing requirement in the preceding year plus estimates of any additional capital financing requirement for the current and next two financial years. This is a key indicator of prudence and was changed from Net Borrowing to gross borrowing under the update to the Codes in 2017.
- Prudential indicator 12 relates to actual external debt at 31st March, which will be reported in the Treasury Management Annual Report.
- Indicators 14 and 15 are no longer explicit within the updated codes however these have been but have been retained pending further review
- Indicator 17 relates solely to Treasury Management investments made under Section 12 of the Local Government act 2003