ROTHERHAM BOROUGH COUNCIL – REPORT TO AUDIT COMMITTEE

1.	**Meeting:**	**Audit Committee**
2.	**Date:**	**30 October 2013**
3.	**Title:**	**Mid Year Treasury Management and Prudential Indicators Monitoring Report 2013/14**
4.	**Directorate:**	**Resources**

5. Summary

Revisions to the regulatory framework of treasury management during 2009 introduced a requirement that the Council receive a mid year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report required previously.

This report meets that revised requirement. It also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council's prudential indicators (PIs).

The report is structured to highlight the key changes to the Council's capital activity (the PIs), the economic outlook and the actual and proposed treasury management activity (borrowing and investment).

6. Recommendations

The Audit Committee is asked to:

1. **Note the report and the treasury activity; and**
2. **Refer the report to Cabinet to consider recommending Council approve the changes to the 2013/14 prudential indicators**.

7. Proposals and Details

The Director of Financial Services has delegated authority to carry out treasury management activities on behalf of the Council and this report is produced in order to comply with the CIPFA Code of Practice in respect of Treasury Management in Local Authorities and the "Prudential Code".

8. Finance

Treasury Management forms an integral part of the Council's overall financial arrangements.

The assumptions supporting the capital financing budget for 2013/14 and for future years covered by the Council's MTFS were reviewed in light of economic and financial conditions and the future years' capital programme.

The Treasury Management and Investment Strategy is not forecast to have any further revenue consequences other than those identified and planned for in both the Council's 2013/14 Revenue Budget and approved MTFS.

9. Risks and Uncertainties

Regular monitoring will ensure that risks and uncertainties are addressed at an early stage and hence kept to a minimum.

10. Policy and Performance Agenda Implications

Effective treasury management will assist in delivering the Council's policy and performance agenda.

11. Background Papers and Consultation

CIPFA Code of Practice for Treasury Management in Local Authorities
Local Government Act 2003
CIPFA "Prudential Code"

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Appendix

Mid Year Prudential Indicators and Treasury Management Monitoring Report

1. Introduction and Background to the Report

1.1 Revisions to the regulatory framework of treasury management during 2009 introduced a requirement that the Council receive a mid year treasury review, in addition to the forward looking annual treasury strategy and backward looking annual treasury report required previously.

1.2 This report meets that revised requirement. It also incorporates the needs of the Prudential Code to ensure adequate monitoring of the capital expenditure plans and the Council's prudential indicators (PIs). The Treasury Strategy and PIs were previously reported to Audit Committee and Cabinet in February 2013 and approved by Council on 6 March 2013.

1.3 The Council's revised capital expenditure plans (Section 2.2 of this report) and the impact of these revised plans on its financing are set out in Section 2.3. The Council's capital spend plans provide a framework for the subsequent treasury management activity. Section 3 onwards sets out the impact of the revised plans on the Council's treasury management indicators.

1.4 The underlying purpose of the report supports the objective in the revised CIPFA Code of Practice on Treasury Management and the CLG Investment Guidance. These state that Members receive and adequately scrutinise the treasury management service.

1.5 The underlying economic and financial environment remains difficult for the Council, foremost being the improving, but still challenging, concerns over investment counterparty risk. This background encourages the Council to continue maintaining investments short term and with high quality counterparties. The downside of such a policy is that investment returns remain low.

1.6 The Director of Financial Services can report that the basis of the treasury management strategy, the investment strategy and the PIs are not materially changed from that set out in the approved Treasury Management Strategy (March 2013).

2. Key Prudential Indicators

2.1. This part of the report is structured to update:

- The Council's capital expenditure plans;
- How these plans are being financed;
- The impact of the changes in the capital expenditure plans on the PIs and the underlying need to borrow; and
- Compliance with the limits in place for borrowing activity.

2.2 **Capital Expenditure (PI)**

2.2.1 This table shows the revised estimates for capital expenditure and the changes since the capital programme was agreed at the Budget. The revised estimate reflects the latest position in the 2013/14 capital monitoring report presented to Cabinet on 16 October 2013

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Capital Expenditure by Service	2013/14 Original Estimate £m	2013/14 Revised Estimate £m
Children & Young People's Services	9.906	20.493
Environmental & Development Services	16.954	25.536
Neighbourhoods & Adult Services – Non-HRA	3.419	4.292
Resources	1.260	2.280
Total Non-HRA	**31.539**	**52.601**
Neighbourhoods & Adult Services – HRA	30.228	32.307
Total HRA	**30.228**	**32.307**
Total	**61.767**	**84.908**

2.3 **Impact of Capital Expenditure Plans**

2.3.1 **Changes to the Financing of the Capital Programme**

The table below draws together the main strategy elements of the capital expenditure plans (above), highlighting the expected financing arrangements of this capital expenditure.

Capital Expenditure	2013/14 Original Estimate £m	2013/14 Revised Estimate £m
Total spend	61.767	84.908
Financed by:		
Capital receipts	1.412	1.775
Capital grants, capital contributions & other sources of capital funding	51.599	69.154
Borrowing Need	8.756	13.979
Total Financing	**61.767**	**84.908**
Supported Borrowing	0.188	0.000
Unsupported Borrowing	8.568	13.979
Borrowing Need	**8.756**	**13.979**

The borrowing element of the table increases the underlying indebtedness of the Council by way of the Capital Financing Requirement (CFR), although this will be reduced in part by revenue charges for the repayment of debt (the Minimum Revenue Provision). This direct borrowing need may also be supplemented by maturing debt and other treasury requirements.

2.3.2 As reported to Audit Committee in July 2013 actual expenditure financed by borrowing in 2012/13 was £7.643m less than anticipated. The increase in borrowing need for 2013/14 therefore reflects both the re-profiling of projects within the approved capital programme and new approvals.

2.3.3 **Changes to the Capital Financing Requirement (PI), External Debt and the Operational Boundary (PI)**

The table below shows the CFR, which is the underlying external need to borrow for a capital purpose. It also shows the expected debt position over the period. This is termed the Operational Boundary which was set at the beginning of the financial year at £602.844m.

2.3.4 **Prudential Indicators – Capital Financing Requirement & External Debt / the Operational Boundary**

In addition to showing the underlying need to borrow, the Council's CFR has since 2009/10, also included other long term liabilities which have been brought on balance sheet, for example, PFI schemes and finance lease assets. No borrowing is actually required against these schemes as a borrowing facility is already included in the contract. The estimate for 2013/14 does not require any revision as there is no change in the borrowing need from such arrangements.

2.3.5 As actual capital expenditure financed by borrowing in 2012/13 was £7.643m less than anticipated this resulted in an overall year-end CFR of £755.036m compared to the £762.679m estimated. Whilst the revised CFR for 2013/14 of £756.960m is less than originally estimated (£759.101m) the figure represents an increase of £1.924m when compared to the 2012/13 year-end position.

RMBC	2013/14 Original Estimate £m	Current Position £m	2013/14 Revised Estimate £m
Prudential Indicator – Capital Financing Requirement			
CFR – Non Housing	324.737		322.596
CFR – Housing	306.959		306.959
Total CFR excluding PFI, finance leases and similar arrangements	631.696		629.555
Net movement in CFR	-1.645		3.857
Cumulative adjustment for PFI, finance leases and similar arrangements	127.405		127.405
Net movement in CFR	-1.933		-1.933
Total CFR including PFI, finance leases and similar arrangements	759.101		756.960
Net movement in overall CFR	-3.578		1.924
Prudential Indicator – External Debt / the Operational Boundary			
Borrowing	475.439	487.301	490.020
Other long term liabilities*	127.405	127.405	127.405
Total Debt 31 March	602.844	614.706	617.425

* - Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

Former SYCC	2013/14 Original Estimate £m	Current Position £m	2013/14 Revised Estimate £m
Prudential Indicator – External Debt / the Operational Boundary			
Borrowing	96.121	96.121	96.121
Other long term liabilities	0	0	0
Total Debt 31 March	96.121	96.121	96.121

3. <u>Limits to Borrowing Activity</u>

3.1 The first key controls over the treasury activity is a PI to ensure that over the medium term, gross and net borrowing will only be for a capital purpose. Gross and net external borrowing should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for 2013/14 and next two financial years. This allows some flexibility for limited early borrowing for future years. The Council has approved a policy for borrowing in advance of need which will be adhered to if this proves prudent to do so.

RMBC	2013/14 Original Estimate £m	Current Position £m	2013/14 Revised Estimate £m
Gross Borrowing	475.439	487.301	490.020
Plus Other Long Term liabilities*	127.405	127.405	127.405
Total Gross Borrowing	602.844	614.706	617.425
CFR*	759.101	755.998	756.960
Total Gross Borrowing	602.844	614.706	617.425
Less Investments	10.000	30.300	20.000
Net Borrowing	592.844	584.406	597.425
CFR*	759.101	755.998	756.960

* - Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

3.2 The Director of Financial Services reports that no difficulties are envisaged for the current or future years in complying with this PI.

3.3 A further PI controls the overall level of borrowing. This is the Authorised Limit which represents the limit beyond which borrowing is prohibited, and needs to be set and revised by Members. It reflects the level of borrowing which, while not desired, could be afforded in the short term, but is not sustainable in the longer term. It is the expected maximum borrowing need with some headroom for unexpected movements. This is the statutory limit determined under section 3 (1) of the Local Government Act 2003.

Authorised limit for external debt (RMBC)	2013/14 Original Indicator £m	Current Position £m	2013/14 Revised Indicator £m
Borrowing	633.597	487.301	631.456
Other long term liabilities*	127.405	127.405	127.405
Total	761.002	614.706	758.861

* - Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

Authorised limit for external debt (Former SYCC)	2013/14 Original Indicator £m	Current Position £m	2013/14 Revised Indicator £m
Borrowing	100.000	96.121	100.000
Other long term liabilities	0.000	0.000	0.000
Total	100.000	96.121	100.000

4. Treasury Strategy 2013/14 – 2015/16

4.1 Debt Activity during 2013/14

4.1.1 The expected borrowing need is set out below:

RMBC	2013/14 Original Estimate £m	Current Position £m	2013/14 Revised Estimate £m
CFR	759.101	755.998	756.960
Less Other Long Term Liabilities*	127.405	127.405	127.405
Net Adjusted CFR (y/e position)	631.696	628.593	629.555
Borrowed at 30/09/13	478.222	487.301	487.301
Under borrowing at 30/09/13	153.474	141.292	142.254
Borrowed at 30/09/13	478.222		487.301
Estimated to 31/03/14	-2.783		2.719
Total Borrowing	475.439		490.020
Under borrowing at 31/03/14	156.257		139.535

* - Includes on balance sheet PFI schemes, finance leases and similar arrangements, etc.

4.1.2 The Council is currently under-borrowed. The delay in borrowing reduces the cost of carrying the borrowed monies when yields on investments are low relative to borrowing rates. There is also an interest rate risk, as longer term borrowing rates may rise, but this position is being closely monitored and the overall position carefully managed.

4.1.3 During the six months to 30 September 2013 the Council has not borrowed any amounts on a long-term basis

4.1.4 During the six months to 30 September 2013, the Council has repaid the following amounts:

Lender	Principal	Type	Interest Rate
PWLB	£1,000,000	Fixed rate (EIP)	3.46%
PWLB	£65,000	Fixed rate (EIP)	3.79%
PWLB	£71,180	Fixed rate (Annuity)	Various

One EIP loan for £20m is being repaid in equal half yearly instalments of £1m over its 10 year term. A second EIP loan is for £1.3m which is being repaid in equal half yearly instalments of £65,000 over its 10 year term. There are 5 Annuity loans on which variable amounts of principal are repaid each six months.

4.1.5 There has been no restructuring or early repayment of existing debt in the first six months of 2013/14.

5. Investment Strategy 2013/14 – 2015/16

5.1 Key Objectives

The primary objective of the Council's investment strategy is the safeguarding the repayment of the principal and interest of its investments on time – the investment return being a secondary objective. The current difficult economic and financial climate has heightened the Council's over-riding risk consideration with regard to "Counterparty Risk". As a result of these underlying market concerns officers continue to implement an operational investment strategy which further tightens the controls already in place in the approved investment strategy.

5.2 **Current Investment Position**

The Council held £30.3m of investments at 30 September 2013 (excluding Icelandic Banks), and the constituent parts of the investment position are:

Sector	Country	Up to 1 year £m	1 - 2 years £m	2 – 3 years £m
Banks	UK	0	0	0
DMO	UK	30.300	0	0
Local Authorities	UK	0	0	0
Total		30.300	0	0

5.3 **Risk Benchmarking**

A regulatory development is the consideration and approval of security and liquidity benchmarks. Yield benchmarks are currently widely used to assess investment performance. Discrete security and liquidity benchmarks are new requirements to the Member reporting.

The following reports the current position against the benchmarks.

5.3.1 **Security** – The Council monitors its investments against historic levels of default by continually assessing these against the minimum criteria used in the investment strategy. The Council's approach to risk, the choice of counterparty criteria and length of investment ensures any risk of default is minimal when viewed against these historic default levels.

5.3.2 **Liquidity** – In respect of this area the Council set liquidity facilities/benchmarks to maintain:

- A Bank overdraft facility of £10m
- Liquid short-term deposits of at least £3m available within a week's notice.

The Director of Financial Services can report that liquidity arrangements were adequate during the year to date.

5.3.3 **Yield** – a local measure for investment yield benchmark is internal returns above the 7 day LIBID rate

The Director of Financial Services can report that the return to date averages 0.25%, against a 7 day LIBID to end September 2013 of 0.36%. This is reflective of the Council's current approach to risk whereby security has been maximised by using the Debt Management Office and other Local Authorities as the principal investment counterparties.

6. Revisions to the Investment Strategy

6.1 The counterparty criteria are continually under regular review but in the light of the current market conditions no recommendations are being put to Members to revise the Investment Strategy.

7. Treasury Management Prudential Indicators

7.1 **Actual and estimates of the ratio of financing costs to net revenue stream**

This indicator identifies the trend in the cost of capital (financing costs net of interest and investment income) against the net revenue stream.

	2013/14 Original Indicator %	2013/14 Revised Indicator %
Non-HRA	7.94	7.84
HRA	18.36	18.13

7.2 The revised non HRA indicator reflects the impact of borrowing being at rates less than originally anticipated for 2013/14. The HRA indicator has increased slightly due to the final HRA revenue budget being less than that assumed in the original indicator.

7.3 **Prudential indicator limits based on debt net of investments**

- **Upper Limits On Fixed Rate Exposure** – This indicator covers a maximum limit on fixed interest rates.

- **Upper Limits On Variable Rate Exposure** – Similar to the previous indicator this identifies a maximum limit for variable interest rates based upon the debt position net of investments.

RMBC	2013/14 Original Indicator	Current Position	2013/14 Revised Indicator
Prudential indicator limits based on debt net of investments			
Limits on fixed interest rates based on net debt	100%	94.53%	100%
Limits on variable interest rates based on net debt	30%	5.47%	30%

7.4 **Maturity Structures Of Borrowing**

These gross limits are set to reduce the Council's exposure to large fixed rate loans (those instruments which carry a fixed interest rate for the duration of the instrument) falling due for refinancing.

Unlike previous years the indicator and current position shown below now reflect the next call dates on the Council's LOBO loans rather then the actual maturity date of those loans. This gives a better indication of risk and whilst there is a possibility that a loan is called with an increase in interest payable the likelihood of any LOBO loans being called in the current climate is assessed as zero for the next three years.

RMBC	2013/14 Original Indicator		Current Position	2013/14 Revised Indicator	
	Lower	Upper		Lower	Upper
Maturity Structure of fixed borrowing					
Under 12 months	0%	35%	18.85%	0%	35%
12 months to 2 years	0%	35%	10.23%	0%	35%
2 years to 5 years	0%	40%	22.04%	0%	40%
5 years to 10 years	0%	40%	16.73%	0%	40%
10 years to 20 years	0%	45%	4.89%	0%	45%
20 years to 30 years	0%	50%	7.52%	0%	50%
30 years to 40 years	0%	50%	5.52%	0%	50%
40 years to 50 years	0%	55%	14.24%	0%	55%
50 years and above	0%	60%	0.00%	0%	60%

The former SYCC account is due to be wound up by the end of 2020/21 and the maturity structure is now largely fixed as the need and indeed opportunities to re-finance within the remaining 10 years will be limited. As a result future limits are currently set in line with the on-going maturity profile.

Former SYCC	2013/14 Original Indicator		Current Position	2013/14 Revised Indicator	
	Lower	Upper		Lower	Upper
Maturity Structure of fixed borrowing					
Under 12 months	0%	50%	0.00%	0%	50%
12 months to 2 years	0%	70%	0.00%	0%	70%
2 years to 5 years	0%	100%	61.51%	0%	100%
5 years to 10 years	0%	100%	38.49%	0%	100%

7.5 **Total Principal Funds Invested**

These limits are set to reduce the need for the early sale of an investment, and show limits to be placed on investments with final maturities beyond each year-end.

The Council currently has no sums invested for periods exceeding 364 days due to market conditions. To allow for any changes in those conditions the indicator has been left unchanged. The above also excludes any Icelandic investments that are due to be recovered after more than 364 days.

RMBC	2013/14 Original Indicator £m	Current Position £m	2013/14 Revised Indicator £m
Maximum principal sums invested > 364 days	10	0	10
Comprising			
Cash deposits	10	0	10

8. Treasury Management Advisors

8.1 Re-appointment of Treasury and Asset Finance Advisors

The Council's three year contract with Sector Treasury Services for the provision of treasury management and asset finance services expired on 6 October 2013.

In accordance with the Council's Standing Orders, a tendering exercise has been carried out for the re-procurement of these services for a further three year period.

An open tender exercise was held from which two submissions were received – one from Sector Treasury Services (now trading as Capita Asset Services Treasury Solutions) and a second from Arlingclose.

These were evaluated on quality and price with Capita Asset Services Treasury Solutions bid ranking slightly higher on both criteria.

Accordingly, a decision has been taken to re-appoint Capita Asset Services Treasury Solutions for a further term of three years with effect from 7 October 2013.

The cost of the contract over the 3 year period is £16,000 in year 1, £16,500 in year 2 and £17,000 in year 3. The annual cost in the final year of the three year contract which has just expired was £16,500.