13 February 2013	ITEM : 17 01104188
Cabinet	
BORROWING AND INVESTMENT ANNUAL STRATEGY AND THE ANNUAL MINIMUM REVENUE PROVISION STATEMENT 2013/14	
Portfolio Holder: Councillor John Kent, Portfolio Holder for Finance and Strategy	
Wards and communities affected: All	**Key Decision:** Yes
Accountable Head of Service: Sean Clark, Head of Corporate Finance	
Accountable Director: Martin Hone, Director of Finance and Corporate Governance	
This report is Public	
Purpose of Report: To recommend the Treasury Management Strategy for 2013/14, including the Prudential Indicators, to Council.	

EXECUTIVE SUMMARY

The CIPFA Code of Practice for Treasury Management in Public Services and the Prudential Code requires local authorities to determine the Treasury Management Strategy and Prudential Indicators on an annual basis. The annual strategy also includes the Annual Investment Strategy that is a requirement of the Department for Communities and Local Government Investment Guidance.

In accordance with the above Codes, this report:

a) makes proposals for the Prudential Indicators for 2013/14;

b) reviews borrowing and investment strategies for 2013/14; and

c) sets out a draft Treasury Management budget for 2013/14.

The borrowing limits are determined for statutory purposes and to maximise flexibility. They do not mean that the Council will necessarily borrow up to the amounts specified.

1 RECOMMENDATIONS:

1.1 **That the Cabinet recommend that the Council:**

a) Agree the Prudential Indicators as set out in Appendix 1;

b) Delegate any changes to the Prudential Indicators to Cabinet where changes are required due to the delivery mechanism for affordable homes in the borough;

c) Agree the Annual Borrowing and Investment Strategy in paragraph 2.33;

d) To approve the Annual Borrowing and Investment Strategy and the Annual Minimum Revenue Provision (MRP) Statement for 2013/14 as follows;

- **For debt where the government provides revenue support the Council will set aside 4% of the notional debt relating to capital investment, but excluding capital investment on the HRA housing stock (known as the non-HRA capital financing requirement;**

- **For debt where the government provides no revenue support: - where the debt relates to an asset the Council will set aside a sum equivalent to repaying debt over the life of the asset in equal instalments, or where the debt relates to expenditure which is subject to a capitalisation direction issued by the government the Council will set aside a sum equivalent to repaying debt over a period consistent with the nature of the expenditure; and**

e) To note the revised 2012/13 and 2013/14 borrowing and investment projections as set out in the report (paragraph 2.35).

2 INTRODUCTION AND BACKGROUND:

2.1 This Borrowing and Investment Annual Strategy and Annual MRP Statement is prepared under the terms of the CIPFA Prudential Code for Capital Finance in Local Authorities (the code) and seeks approval for the Prudential Indicators in accordance with the Code. CIPFA revised the Treasury Management Code and Guidance Notes as well as the Prudential Indicators in late 2011. The Council has had regard to all these documents in compiling this report.

2.2 The report also revises the 2012/13 forecast for interest on borrowing and investment and forecasts the 2013/14 indicative interest payable and receivable.

Borrowing Activity 2012/13 and 2013/14

2.3 The underlying need to borrow for capital purposes, as measured by the Capital Financing Requirement (CFR), together with balances and reserves, are the core drivers of Treasury Management activity. The estimates, based on the current revenue budget and capital programmes are:

	31/3/2013 Estimate £m	31/3/2014 Estimate £m	31/3/2015 Estimate £m
General Fund CFR	129.3	135.1	133.2
HRA CFR (includes effects of Housing Finance Reform based on current available figures)	166.0	166.0	166.0
TOTAL CFR	**295.3**	**301.1**	**299.2**
Less: Existing profile of borrowing and other long term liabilities	286.3	285.3	285.3
Cumulative maximum External Borrowing Requirement	**9.0**	**15.8**	**13.9**
Balances and Reserves	11.7	12.5	12.5
Cumulative Net Borrowing Requirement	**-2.7**	**3.3**	**1.4**

2.4 The Council's level of physical debt and investments is linked to these components of the balance sheet. Market conditions, interest rate expectations and credit risk considerations will influence the Council's strategy in determining the borrowing and investment activity against the underlying balance sheet position. The Council will ensure that net physical external borrowing will not exceed the CFR other than for short term cashflow requirements.

2.5 In conjunction with advice from its treasury advisor, Arlingclose Ltd, the Council will keep under review the following borrowing options:

- PWLB loans;
- Borrowing from other Local Authorities;
- Borrowing from institutions such as the European Investment Bank and from commercial banks;
- Borrowing from the money markets;
- Capital Markets (stock issues, commercial paper and bills);
- Local authority stock issues;
- Local Authority bills;
- Structured finance; and
- Internal sources.

2.6 The PWLB issued circular 147 on 20 October 2010 following the Comprehensive Spending Review (CSR) announcement which increased the cost of new local authority fixed rate loans to 1% above the cost of Government borrowing. This was counteracted in part by the introduction of the Public Works Loan Board (PWLB) Certainty Rate in circular 153 on 16 October 2012 that reduced PWLB rates by 0.20%. The PWLB remains an attractive source of borrowing, given the transparency and control that its facilities continue to provide. The types of PWLB borrowing that are considered appropriate for a low interest rate environment are:

- Variable rate borrowing;
- Medium-term equal instalments of principal (EIP) or annuity loans; and
- Long term loans, where affordable.

2.7 Treasury management and borrowing strategies in particular continue to be influenced not only by the absolute level of borrowing rates, but also the relationship between short and long term interest rates. This difference creates a ‘cost of carry’ for any new longer term borrowing where the proceeds are temporarily held as investments because of the difference between what is paid on the borrowing and what is earned on the investment. The cost of carry is likely to be an issue until 2016 and beyond. As borrowing is often for longer dated periods the cost of carry needs to be considered against a backdrop of uncertainty and affordability constraints in the authority’s wider financial position.

2.8 The cost of carry has resulted in an increased reliance upon shorter dated and variable rate borrowing. This type of borrowing injects volatility into the debt portfolio in terms of interest rate risk, but is counterbalanced by its affordability and alignment of borrowing costs with investment returns. The authority’s exposure to shorter dated and variable rate borrowing is kept under regular review by reference to the difference or spread between variable rate and longer term borrowing costs. A significant narrowing in the spread (e.g. by 0.50%) will result in an immediate and formal review of the borrowing strategy to determine whether the exposure to shorter dated and variable rates is maintained or altered.

2.9 The Council has £29 million of loans which are LOBO loans (Lenders Option Borrowers Option) all of which are in their call period. In the event the lender exercises the option to change the rate or terms of the loan, the Council will consider the terms being provided and also repayment of the loan without penalty. The Council may utilise cash resources for repayment or may consider replacing the loan(s) by borrowing from the PWLB or capital markets. As the current rates on these loans are significantly above base rates it is unlikely that the lenders will exercise their option. The Council will also investigate any possibility of premature repayment of these loans with any final decisions being taken having due regard to any premium costs associated with each loan.

2.10 The rationale for the rescheduling of any loans would be one or more of the following:

- Reduce investment balances and credit exposure via debt repayment;

- Align long-term cash flow projections and debt levels;
- Savings in risk adjusted interest costs;
- Rebalancing the interest rate structure of the debt portfolio; and
- Changing the maturity profile of the debt portfolio.

2.11 Borrowing and rescheduling activity will be reported to both the Audit Committee and Cabinet on a regular basis during 2013/14.

2.12 In August 2010 the Council repaid its entire PWLB portfolio of loans (£84 million) to obtain significant interest savings. The re-financing was undertaken by utilising short term funds from the money markets, mainly other Local Authorities, at substantially lower rates than taking longer term fixed debt. It is envisaged that with the current outlook for interest rates that financing from short term money market debt will continue in 2013/14 and probably beyond. It is recognised that this policy does present on-going risk with regard to potentially higher rates and increased debt costs in the future.

2.13 However, this was weighed against the reality of holding fixed rate debt, at a substantial margin above short term rates, for what could prove to be a prolonged period. Borrowing can be swiftly re-fixed if required via the PWLB, either in total within a matter of days of the decision to re-fix being made or profiled against the maturity schedule of the short term debt. While it is inevitable that interest rates will eventually rise and inflation remains above target, it is the current assessment that official rate increases will not occur until well into 2016. Officers and the Council's advisors will continue to closely monitor the situation to ensure any action is taken as and when required.

2.14 Based on this outlook, officers are working on a plan for a phased move away from temporary debt from April 2015 and the increased costs have been included within the Medium Term Financial Strategy (MTFS) to reflect this.

2.15 Housing Finance Reform – Central Government completed its reform of the Housing Revenue Account Subsidy system at the end of 2011/12. Local authorities are required to recharge interest expenditure and income attributable to the HRA in accordance with determinations issued by the Department for Communities and Local Government. The determinations do not set out a methodology for calculating the interest rate to use in each instance. The Council is therefore required to adopt a policy that will set out how interest charges attributable to the HRA will be determined. The CIPFA Code recommends that authorities present this policy in their TMSS.

2.16 On 1 April 2012, the Council notionally split each of its existing long-term loans into General Fund and HRA pools. In the future, new long-term loans borrowed will be assigned in their entirety to one pool or the other. Interest payable and other costs/income arising from long-term loans (e.g. premiums and discounts on early redemption) will be charged/credited to the respective revenue account. Differences between the value of the HRA loans pool and the HRA's underlying need to borrow (adjusted for HRA balance sheet resources available for investment) will result in a notional cash balance which may be positive or negative. This balance will be measured and interest transferred between the General Fund and HRA at an internally determined rate of interest.

2.17 The Housing Finance Reform has meant that, despite the increased debt and related costs, the HRA will generate surpluses in excess of £6m per annum. The HRA budget reports demonstrate two uses for this funding:

- Existing Stock – there is to be a significant increase in the amounts set aside to refurbish existing stock through the capital programme; and
- New Stock – the Council has made clear an aspiration to create 200 new affordable homes per annum. The delivery body of these homes is still being determined due to likely mixed tenure and borrowing restrictions within the HRA – as such, Council are asked to delegate changes to the prudential indicators to Cabinet, for this purpose only, to allow this development to take place. Such changes would be required in terms of the Council's borrowing activity with a likely increase over the period of development.

Investments

2.18 Guidance from the Department of Communities and Local Government (DCLG) on Local Government Investments in England requires that an Annual Investment Strategy (AIS) be set.

2.19 The Council's investment priorities are:

- Security of the invested capital being paramount;
- Liquidity of the invested capital; and
- An optimum yield which is commensurate with security and liquidity.

2.20 Investments are categorised as 'Specified' or 'Non Specified' investments based on the criteria in the DCLG guidance. Potential Instruments for the Council's use within its Investment Strategy are contained in Appendix 2 for Specified Investments and Appendix 3 for Non Specified Investments.

2.21 Changes to the investment strategy for 2013/14 include:

- The introduction of Singapore as a non-UK country with the use of DBS Bank, Overseas Chinese Banking Corporation and the United Overseas Bank as investment Counterparties;
- The use of the Finnish bank, Pohjola Bank as an investment counterparty;
- The introduction of Registered Providers (RP's) as an investment counterparty; and
- The introduction in the non-specified category of an entry to include organisations that do not meet the specified criteria upon agreement of the Director of Finance and Corporate Governance. See paragraph 2.24.

2.22 The Council's in-house investments are made with reference to the outlook for the UK Bank rate, money market rates and cashflow and the Council selects countries and the institutions within them for the counterparty list after analysis and careful monitoring of:

- Credit Ratings (minimum long-term A- for counterparties; AA+ for non-UK countries);
- Credit default swaps (where quoted);

- GDP; Net debt as percentage of GDP and other economic fundamentals;
- Sovereign support mechanisms/potential support for a well-resourced parent institution;
- Share prices;
- Subjective overlay or put more simple common sense; and
- Corporate developments, news articles, market sentiment.

2.23 Any institution can be suspended or removed should any of the factors identified give cause for concern. It remains the Authority's policy to make exceptions to counterparty policy established around credit ratings but this is conditional and directional. What this means is that an institution that meets the criteria may be suspended, but institutions not meeting the criteria will not be added.

2.24 During 2012/13 the authority has been investigating ways to increase investment income. In 2013/14 the inclusion of organisations that do not meet the minimum credit rating criteria for investment has been included in the non-specified investment category upon agreement from the Director of Finance and Corporate Governance. To this end the Council will invest with its own bankers, the Co-Operative Bank, and also all Building Societies in 2013/14. Details of credit limits have been include in Appendix 3 for Non-Specified Investments.

2.25 With short term interest rates low for even longer, an investment strategy will typically result in the lengthening of investment periods, where cash flow permits, in order to lock into higher interest rates. The problem in the current climate is finding an investment counterparty providing acceptable levels of counterparty risk. The Authority will therefore diversify its portfolio into a range of approved investment counterparties in order to achieve a diversified portfolio of prudent counterparties, investment periods and rates of return. Maximum investment levels with each counterparty will be set to ensure prudent diversification is achieved.

2.26 The Council continues to use Investec as Fund Managers with £15 million in Investec's Segregated Fund and £5 million in Investec's Target Return and Short Dated Bond Fund (previously called the Cash Plus Fund).

2.27 Local Authorities have previously made use of financial derivatives embedded into loans and investments both to reduce interest rate risk and to reduce costs or increase income at the expense of greater risk. The general power of competence in Section 1 of the Localism Act 2011 removes much of the uncertainty over Authorities use of standalone financial derivatives. The CIPFA code requires authorities to clearly detail their policy on the use of derivatives in the annual strategy.

2.28 The Authority will only use standalone derivatives (such as swaps, forward, futures and options) where they can be clearly demonstrated to reduce the overall level of financial risks that the Authority is exposed to. Additional risks presented, such as credit exposure to derivative counterparties, will be taken into account when determining the overall level of risk. Embedded derivatives will not be subject to this policy, although the risks they present will be managed in line with the overall treasury risk management strategy.

2.29 Financial derivative transactions may be arranged with any organisation that meets the approved investment criteria. The current value of any amount due from a derivative counterparty will count against the counterparty credit limit and the relevant foreign country limit. The local authority will only use derivatives after seeking expertise, a legal opinion and ensuring officers have the appropriate training for their use.

2.30 The Authority complies with the provisions of S32 of the Local Government Finance Act 1992 to set a balanced budget.

Annual Borrowing and Investment Strategy and Annual MRP Statement

2.31 Local Authorities are required to prepare an Annual Statement of their policy on making MRP for each financial year. Appendix 4 outlines the assessment of the Council's Annual MRP Statement for 2013/14, which is included as item (i) in the Annual Strategy in paragraph 2.33.

2.32 Officers have reviewed the current strategy and recommend that no revisions are made to the strategy for 2013/14.

2.33 Therefore, with regards to the foregoing paragraphs on Borrowing Activity and Investments the following statement forms the Council's Borrowing and Investment Strategy with effect from 1 April 2013:

a) To obtain any long term borrowing requirement from the sources of finance mentioned in paragraph 2.5;

b) To continue to fund the ex-PWLB debt via short term funds from the money markets unless circumstances dictate moving back into long term fixed rate debt. The borrowing sources mentioned in paragraph 2.5 will then be assessed as to their suitability for use.

c) Repay market loans that come up for renewal by realising equivalent amounts of investments. If it is not possible to realise investments then the borrowing sources in paragraph 2.5 will be assessed as to their suitability for use as replacements.

d) To undertake short term temporary borrowing when necessary in order to manage cash flow to the Council's advantage.

e) Reschedule market and PWLB loans, if practicable, to achieve interest rate reductions, balance the volatility profile or amend the debt profile, dependent on the level of premiums payable or discounts receivable.

f) Ensure security and liquidity of the Council's investments and to then optimise investment returns commensurate to those ideals.

g) Contain the type, size and duration of investments with individual institutions within the limits specified in Appendix 2 and Appendix 3.

h) Move a further £5 million into Investec's Short Dated Bond Fund and Target return Fund if it is felt prudent to do so;

i) In accordance with the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 the Council's policy for the calculation of MRP in 2013/14 shall be the regulatory method for supported borrowing and the asset life (equal instalment) method for Prudential borrowing.

Interest Projections 2012/13 Revised and 2013/14 Original

2.34 The CIPFA document Treasury Management in the Public Services: Code of Practice places a requirement on Council to publish estimates relating to the operation of the borrowing and investment function.

2.35 The Revised 2012/13 budget and the current position at 31 December 2012 and also an initial projection for 2013/14 are shown in summary format in table 2 below: -

		Revised 2012/13 £000's	Month 9 2012/13 £000's	Original 2013/14 £000's
	Expenditure			
	Interest payable on External Debt			
1.	Debt Interest	4,507.0	2,603.8	2,687.8
2.	Discounts/Premiums	188.5	188.5	188.5
3.	Prudential Borrowing Credits	-760.5	-760.5	-967.3
4.	Total interest payable	3,935.0	2,031.8	1,909.0
5.	Internal Interest Payable	-106.9	59.0	59.0
6.	Net Interest charged to General Fund	3,828.1	2,090.8	1,968.0
	Income			
7.	Interest on Investments	-454.0	-499.5	-410.3
8.	Net interest charged to General Fund	3,374.1	1,591.3	1,557.7
9.	MRP- Supported Borrowing	4,301.3	4,220.0	4031.8
10.	Treasury Management expenses	150.0	150.0	150.0

2.36 It should also be noted that the figures shown above for 2013/14 are based on assumptions made about the level of balances available for investment, any anticipated new long term borrowing and the level of interest rates achievable. They are therefore liable to be subject to a significant degree of change during the year arising from variations in interest rates and other market and economic developments, and officers' response to those events.

2.37 In accordance with the requirements of the revised CIPFA Treasury Management Code, the Council will report on treasury management activity and the outturn against the treasury related Prudential Indicators at least twice a year, one such report will be after the financial year end.

3 ISSUES, OPTIONS AND ANALYSIS OF OPTIONS:

3.1 There is very little in terms of options as the policies are largely set out by guidance and legislation and prudential indicators are governed by decisions around the revenue and capital budgets.

3.2 There are two key areas in this report for Members to be particularly mindful of:

a) The plan to maintain temporary borrowing for the next two financial years and implement a plan of a phased move away from temporary debt from 2015/16. Officers will continue to monitor this to react to any changes in the economy; and

b) There is a clear commitment and need for affordable housing in the borough and this could impact on the prudential indicators appended to this report through an increase in borrowing.

4 REASONS FOR RECOMMENDATION:

4.1 There is a legal requirement for a Borrowing and Investment Annual Strategy and the Annual Minimum Revenue Provision Statement. This report and appendices has been written in line with best practice and the Council's spending plans.

5 CONSULTATION

5.1 The Council's Treasury Advisors, Arlingclose, have been consulted. As set out in section 4, the report is largely based on best practice and the Council's spending plans that have been scrutinised throughout recent months.

6 IMPACT ON CORPORATE POLICIES, PRIORITIES, PERFORMANCE AND COMMUNITY IMPACT

6.1 Treasury Management plays a significant support role in the delivery of services to the community. Since the debt restructure in August 2010, the function has contributed in the region of £7m to date to reserves and services.

7 IMPLICATIONS

7.1 <u>Financial</u>

Implications verified by: **Chris Buckley**
Telephone and email: **01375 652015**
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The financial implications are included in the main body of the report.

7.2 **Legal**

Implications verified by: **David Lawson**
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The report is in accordance with the Local Government Act 2003, related secondary legislation and other requirements including the Prudential Code.

Publication of the strategies is a statutory requirement and conforms to best practice as required by the CIPFA Code of Practice.

7.3 **Diversity and Equality**

Implications verified by: **Samson DeAlyn**
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There are no direct diversity implications noted in this report

7.4 **Other implications (where significant) – i.e. Section 17, Risk Assessment, Health Impact Assessment, Sustainability, IT, Environmental**

Not applicable

8 CONCLUSION

8.1 The report sets out the Annual Borrowing and Investment Strategy and the Annual Minimum Revenue Provision Statement. The function has again contributed towards protecting front line services and will be used to facilitate the housing development programme for the borough.

BACKGROUND PAPERS USED IN PREPARING THIS REPORT:

- Revised CIPFA Prudential Code
- Revised draft ODPM's Guidance on Local Government Investments
- Revised CIPFA's Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes
- Treasury Management Policy Statement
- 2012/13 Annual Investment Strategy
- Arlingclose's Investment Review.

APPENDICES TO THIS REPORT:

- Appendix 1 – Prudential Indicators
- Appendix 2 – Specified Investments
- Appendix 3 – Non Specified Investments
- Appendix 4 – MRP

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APPENDIX 1

PRUDENTIAL INDICATORS 2013/14 TO 2015/16

The following prudential indicators are recommended to the Council.

A. Prudential indicators for Affordability

In demonstrating the affordability of its capital investment plan the council must:

- Determine the ratio of financing costs (e.g. capital repayments, interest payments, investment income, etc) to net revenue stream for both the Housing Revenue Account (HRA) and non-HRA services for a 3 year period.

- Determine the incremental impact on the council tax and housing rents (in both instances the scope for increases is governed by the Government's ability to limit council tax increases and the current restriction on council rents).

Indicator A1 sets out the ratio of financing costs to net revenue stream. The estimates of financing costs include current commitments and the proposals in this budget report.

A1: Prudential indicator – Estimates of the ratio of financing costs to net revenue stream 2013/14 to 2015/16

Indicator	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate
Non HRA	6.12	6.39	6.31
HRA	24.6	23.2	22.1

Indicators A2 and A3 set out the estimated incremental impact on both the levels of council tax (Band D equivalent) and housing rents of the recommended capital investment plans and funding proposals. The impact has been calculated using the latest projections on interest rates for both borrowing and investments. The impact does not take account of government support included for new borrowing within the formula spending share and housing subsidy.

A2: Prudential indicator – Estimates of the incremental impact of the new capital investment decisions on the council tax 2013/14 to 2015/16

Indicator	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate
Additional annual Council Tax requirement	0.77	13.67	20.30

A3: Prudential indicator – Estimates of the incremental impact of the new capital investment decisions on the average weekly housing rents 2013/14 to 2015/16

Indicator	2013/14 Estimate	2014/15 Estimate	2015/16 Estimate
Addition in average weekly housing rent	1.84	0.0	0.0

B. Prudential indicators for Prudence

B1: Prudential indicator – Gross debt and the capital financing requirement

This is a key indicator of prudence. In order to ensure that over the medium term debt will only be for a capital purpose, the local authority should ensure that debt does not, except in the short term, exceed the total of the capital financing requirement in the preceding year plus estimates of any additional capital financing requirement for the current and next two financial years.

If in any of these years there is a reduction in the capital financing requirement, this reduction is ignored in estimating the cumulative increase in the capital financing requirement which is used for comparison with gross external debt.

The Director of Finance and Corporate Governance reports that the Authority had no difficulty meeting this requirement in 2012/13, nor are there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

Where the gross debt is greater than the capital financing requirement the reasons for this should be clearly stated in the annual treasury management strategy

C. Prudential indicator for Capital Expenditure

Elsewhere in this report is a recommendation for the capital investment plans for the Council over the next three years. Indicator C1 summarises the recommendations within that report. Indicator C2 sets out the estimates of the capital financing requirement over the same period.

C1: Prudential indicator – Estimates of total capital expenditure 2013/14 to 2015/16

Indicator	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Total Non HRA	33,888	23,550	20,802
Total HRA	17,600	13,600	13,600
Total Programme	51,488	37,150	34,402

In considering the capital investment plan the Council has had regard to a number of key issues, namely:

- affordability, e.g. implications for council tax/housing rents
- prudence and sustainability, e.g. implications for external borrowing
- value for money, e.g. option appraisal
- stewardship of assets, e.g. asset management planning
- service objectives, e.g. strategic planning for the authority
- practicality, e.g. achievability of the forward plan.

C2: Prudential indicator – Estimates of capital financing requirement 2013/14 to 2015/16

Indicator	31/03/14 Estimate £'000	31/03/15 Estimate £'000	31/03/16 Estimate £'000
HRA	166,021	166,021	166,021
Non-HRA	135,116	133,264	129,198
Total	301,137	299,285	295,219

The estimates are based on the financing options included in the recommended capital investment programme. The estimates will not commit the Council to particular methods of funding – the actual funding of capital expenditure will be determined after the end of the relevant financial year.

The Council has a number of daily cashflows, both positive and negative, and manages its treasury position in terms of its borrowings and investments in accordance with the approved treasury management strategy and practices. In day to day cash management no distinction can be made between revenue cash and capital cash. External borrowing arises as a consequence of all the financial transactions of the authority and not simply those arising from capital spending. It is possible, therefore, that external debt could exceed the capital financing requirement in the short term.

D. Prudential indicators for External Debt

A number of prudential indicators are required in relation to external debt.

D1: Prudential indicator – Authorised limit 2013/14 to 2015/16

Indicator	2013/14 Estimate £'000	2014/15 Estimate £'000	2015/16 Estimate £'000
Borrowing	375,641	375,641	375,641
Other Long Term Liabilities	2,000	1,800	1,600
Total	377,641	377,441	377,241

The authorised limit is the aggregate of gross borrowing (i.e. before investment) and other long term liabilities such as finance leases. In taking its decisions on the budget report the Council is asked to note that the authorised limit determined for 2012/13 in the above table is a statutory limit required to be determined by full Council under section 3(1) of the Local Government Act 2003.

The authorised limits are consistent with the Council's current commitments, existing plans and the proposals in the budget report for capital expenditure and financing, and with its approved treasury management policy statement and practices. The Corporate Director of Finance and Corporate Governance and the Head of Corporate Finance confirm that they are based on the estimate of most likely, prudent but not worst case scenario, with in addition sufficient headroom over and above this to allow for operational management, for example unusual cash movements. Risk analysis and risk management strategies have been taken into account, as have plans for capital expenditure, estimates of the capital financing requirement and estimates of cashflow requirements for all purposes.

D2: Prudential indicator – Operational boundary 2013/14 to 2015/16

Indicator	**2013/14 Estimate £'000**	**2014/15 Estimate £'000**	**2015/16 Estimate £'000**
Borrowing	350,641	350,641	350,641
Other Long Term Liabilities	2,000	1,800	1,600
Total	352,641	352,441	352,241

The operational boundary is based on the authorised limit but without the additional headroom. The operational boundary represents a key management tool for in-year monitoring by the Corporate Director of Finance and Corporate Governance and Head of Corporate Finance. As with the authorised limit figures for borrowing (gross) and other long term liabilities are separately identified.

The authorised limit and operational boundary separately identify borrowing from other long-term liabilities. The council is recommended to delegate authority to the Corporate Director of Finance and Corporate Governance and the Head of Corporate Finance, within the total limit for any individual year, to effect movement between the separately agreed limits for borrowing and other long term liabilities, in accordance with option appraisal and best value for money for the authority. Any such changes made will be reported to the council at its next meeting following the change.

D3: Prudential indicator – HRA Limit on Indebtedness Under Self Financing

This is otherwise known as the Debt Cap, the absolute level of debt permitted under Self Financing Regulations. The debt cap is set at £188.141m, therefore all debt attributable to the HRA cannot exceed this figure.

E. Prudential indicators for Treasury Management

A number of prudential indicators are required in respect of treasury management. The indicators are based on the council's treasury management strategy and take into account the pre-existing structure of the council's borrowing and investment portfolios.

E1: Prudential indicator – Thurrock Council has adopted the "CIPFA Code of Practice for Treasury Management in the Public Services" within its Financial Standing Orders.

E2: Prudential indicators – Upper limits on interest rate exposure 2013/14 to 2015/16

Indicator	2013/14	2014/15	2015/16
Upper limit on fixed interest rate exposure	100%	100%	100%
Upper limit on variable interest rate exposure	50%	50%	50%

The above percentages are calculated on the net outstanding principal sums (i.e. net of investments). The upper limit of 100% is a consequence of the council maintaining an investment portfolio. Indicator E2a exemplifies the indicator over borrowing and investment.

E2a: Prudential indicators (supplemental) – Upper limits on interest rate exposure 2013/14 to 2015/16

Indicator	2013/14	2014/15	2015/16
Upper limit on borrowing – fixed rate exposure	100%	100%	100%
Upper limit on borrowing – variable rate exposure	50%	50%	50%
Upper limit on investments – fixed rate exposure	100%	100%	100%
Upper limit on investments – variable rate exposure	50%	50%	50%

Indicator E2a is supplemental to Indicator E2 and shows separately the maximum limits for both borrowing and investments. The indicator is not a requirement of the prudential code but it does show more clearly the interest rate exposure limits within which borrowing and investments will be managed. The effect of the limits is the Corporate Director of Finance & Corporate Governance will manage fixed interest rate exposure within the range 0% to 100% for borrowing and within the range 0% to 100% for investments.

E3`; Prudential indicator – Upper and lower limits on the maturity structure of borrowing 2013/14

	Upper Limit	**Lower Limit**
under 12 months	100%	0%
12 months and within 24 months	60%	0%
24 months and within 5 years	60%	0%
5 years and within 10 years	60%	0%
10 years and within 20 years	60%	0%
20 years and within 30 years	60%	0%
30 years and within 40 years	60%	0%
40 years and within 50 years	100%	0%
50 years and above	100%	0%

The limits in Indicator E3 represent the amount of projected borrowing that is fixed rate maturing in each period as a percentage of total projected borrowing that is fixed rate at the start of the period.

E4: Prudential indicator – Principle sums invested for periods longer than 364 days

Indicator	**2013/14 £'000**	**2014/15 £'000**	**2015/16 £'000**
Limit	15,000	15,000	15,000

E5: Prudential indicator – Credit Risk:

- The Council employs Treasury advisors (Arlingclose) who provide monthly updates that consider security, liquidity and yield in that order, when making investment decisions.
- Credit ratings remain an important element of assessing credit risk, but, they are not a sole feature in the Council's assessment of counterparty credit risk

- The Council also considers alternative assessments of credit strength and information on corporate developments and market sentiment towards counterparties. The following key tools are used to assess credit risk:
    - Published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ or equivalent for non-UK sovereigns)
    - Sovereign support mechanisms
    - Credit default swaps (where quoted)
    - Share prices (where available)
    - Economic fundamentals, such as country's net debt as a percentage of its GDP
    - Corporate developments, news, articles, market sentiment and momentum
    - Subjective overlay

The only indicators with prescriptive values remain to be credit ratings. All other indicators of creditworthiness are considered in relative rather than absolute terms

APPENDIX 2

Specified Investments

Specified investments will be those that meet the criteria in the CLG Guidance, i.e. the investment

- is sterling denominated
- has a maximum maturity of one year
- meets the ''high credit quality'' as determined by the Council or is made with the UK government or is made with a local authority in England, Wales, Scotland or Northern Ireland or a parish or community council.
- The making of which is not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146 (i.e. the investment is not loan capital or share capital in a body corporate)

Specified investments identified for the Council's use are:

- Deposits in the DMO's Debt Management Account Deposit Facility
- Deposits with UK local authorities (includes Police/Fire Authorities, Council run Pension Funds)
- Deposits with banks and building societies
- Certificates of deposit with banks and building societies*
- Gilts : (bonds issued by the UK government)*
- Bonds issued by multi lateral development banks*
- Treasury-Bills (T-Bills)
- Local Authority Bills (LA Bills)
- AAA rated Money Market Funds with a Constant Net Asset Value (CNAV)
- AAA rated Money Market Funds with a Variable Net Asset Value (VNAV)
- Other Money Market Funds and Collective Investment Schemes – i.e. credit rated funds which meet the definition of a collective investment scheme as defined in SI 2004 No 534 and SI 2007 No 573

1. * Investments in these instruments will be on advice from the Council's treasury advisor.
2. The use of the above instruments by the Council's fund managers will be by reference to the fund guidelines contained in the agreement between the Council and the individual manager.

For credit rated counterparties, the minimum criteria will be the short term/long term ratings assigned by various agencies which may include Moody's Investors Services, Standard & Poor's and Fitch. The minimum country rating is AA+ (or equivalent) and the minimum institution rating is A- (or equivalent).

The Council will also take into account information on corporate developments and market sentiment towards investment counterparties.

The Council current specified investment listing is as follows:

Instrument	Country	Counterparty	Maximum Investment Limit
Term deposits	UK	DMADF, DMO	No Limit on either institution
Term deposits/Call Accounts	UK	Other UK Local Authorities(inc Police/Fire Authorites, Council run Pension Funds)	£5 million per authority
Term deposits/Call Accounts/CD's	UK	Bank of Scotland (Lloyds Banking Group)	£5 million
Term deposits/Call Accounts/CD's	UK	Lloyds TSB (Lloyds Banking Group)	£5 million
Term deposits/Call Accounts/CD's	UK	Barclays	£5 million
Term deposits/Call Accounts/CD's	UK	HSBC	£5 million
Term deposits/Call Accounts/CD's	UK	Nationwide BS	£5 million
Term deposits/Call Accounts/CD's	UK	Nat West (RBS Group)	£5 million
Term deposits/Call Accounts/CD's	UK	Santander UK plc (Banco Santander Group)	£5 million
Term deposits/Call Accounts/CD's	UK	Royal Bank of Scotland (RBS Group)	£5 million
Term deposits/Call Accounts/CD's	UK	Standard Chartered Bank	£5 million
Term deposits/Call Accounts/CD's	Australia	Australia and NZ Banking Group	£5 million
Term deposits/Call Accounts/CD's	Australia	Commonwealth Bank of Australia	£5 million
Term deposits/Call	Australia	National Australia Bank	£5 million

Accounts/CD's		(National Australia Bank Group)	
Term deposits/Call Accounts/CD's	Australia	Westpac Banking Corp	£5 million
Term deposits/Call Accounts/CD's	Canada	Bank of Montreal	£5 million
Term deposits/Call Accounts/CD's	Canada	Bank of Nova Scotia	£5 million
Term deposits/Call Accounts/CD's	Canada	Canadian Imperial Bank of Commerce	£5 million
Term deposits/Call Accounts/CD's	Canada	Royal Bank of Canada	£5 million
Term deposits/Call Accounts/CD's	Canada	Toronto-Dominion Bank	£5 million
Term deposits/Call Accounts/CD's	Finland	Pohjola	£5 million
Term deposits/Call Accounts/CD's	Finland	Nordea Bank Finland	£5 million
Term deposits/Call Accounts/CD's	France	BNP Paribas	£5 million
Term deposits/Call Accounts/CD's	France	Credit Agricole CIB (Credit Agricole Group)	£5 million
Term deposits/Call Accounts/CD's	France	Credit Agricole SA (Credit Agricole Group)	£5 million
Term deposits/Call Accounts/CD's	France	Societe Generale	£5 million
Term deposits/Call Accounts/CD's	France	Societe Generale	£5 million
Term deposits/Call Accounts/CD's	Germany	Deutsche Bank AG	£5 million
Term deposits/Call Accounts/CD's	Netherlands	ING Bank NV	£5 million
Term deposits/Call	Netherlands	Rabobank	£5 million

Accounts/CD's			
Term deposits/Call Accounts/CD's	Netherlands	Bank Nederlandse Gemeenten	£5 million
Term deposits/Call Accounts/CD's	Singapore	DBS Bank Ltd	£5 million
Term deposits/Call Accounts/CD's	Singapore	Overseas Chinese Banking Corporation (OCBC)	£5 million
Term deposits/Call Accounts/CD's	Singapore	United Overseas Bank (UOB)	£5 million
Term deposits/Call Accounts/CD's	Sweden	Svenska Handelsbank	£5 million
Term deposits/Call Accounts/CD's	Switzerland	Credit Suisse	£5 million
Term deposits/Call Accounts/CD's	USA	JP Morgan	£5 million
Term deposits/Call Accounts/CD's	As Above	Wholly owned subsidiaries of the above banks with an unconditional written guarantee of support from the parent	£5 million
Gilts	UK	DMO	No Limit
T-Bills	UK	DMO	No Limit
LA-Bills	UK	Other UK Local Authorities	No Limit
Bonds	EU	European Investment Bank/Council of Europe	Maximum of £15 million
AAA rated Money Market Funds	UK/Ireland/Luxembourg	CNAV MMFs	Maximum £5 million per fund
Other MMFs and CIS	UK	Collective Investment Schemes	To be decided on an individual basis

Non UK Banks – these are restricted to a maximum exposure of £12,500,000 per country although 100% of the Council's investments may be situated in non UK Banks.

MMF's – For diversification purposes, as far as practicable, investments in Money Market Funds should be spread between two or more funds

Group limits – for institutions that are members of a group there should be no more than £10,000,000 invested in that group at any one time, taking into account individual limits for the institutions concerned.

Maximum duration limits are 2 years for term deposits and instruments without a secondary market and 5 years for negotiable instruments

APPENDIX 3

Non - Specified Investments

Having considered the rationale and risk associated with Non- Specified Investments, the following have been determined for the Council's use:

	In-house use	Use by Fund managers	Maximum Maturity	Maximum % of Portfolio	Capital Expenditure
Investments with organisations which do not meed the specified investment criteria (subject to approval for the Director of Finance and Corporate Governance	Yes	Yes	See Note 3 below	See Note 3 below	No
Term Deposits with banks and Building Societies (which meet the specified criteria)	Yes	Yes	2 years	25% maximum £5 million limit per institution	No
Certificates of Deposit with banks and Building Societies (which meet the specified criteria)	Yes	Yes	5 years	25% maximum £5 million limit per institution	No
Gilts	Yes (on advice from	Yes	10 Years	25%	No

	treasury advisors)				
Deposits with Registerd Providers	Yes	Yes	2 years	25% maximum £5 million limit per institution	No
Bonds issued by Multilateral Development Banks	Yes (on advice from treasury advisors)	Yes	10 Years	25%	No
Bonds issued by financial institutions guaranteed by the UK Government e.g. GEFCO	Yes (on advice from treasury advisors)	Yes	10 Years	25%	No
Sterling denominated bonds by non-UK sovereign governments	Yes (on advice from treasury advisors)	Yes	10 Years	25%	No
Money Market funds and collective investment schemes	Yes (on advice from treasury advisors)	Yes	These funds do not have a defined maturity date	25%	No
Unrated deposit takers (Building Societies only) which do not have an unconditional guarantee	Yes		Currently on an overnight basis only	100% maximum £5 million limit per institution (this means all of the Council's investments could be on an overnight basis with these institutions)	No

Unrated deposit takers (Subsidiary Banks) with an unconditional guarantee from it's Parent	Yes		Max 364 days	100% maximum £5 million per institution within group limits	No
Corporate & debt instruments issued by corporate bodies purchased from 1/4/12 onwards	Yes (on advice from treasury advisors)	Yes	10 Years	25%	No
Collective Investment Schemes (pooled funds) which do not meet the definition of collective investments schemes in SI 2004 No 534 or SI 2007 No 573 and subsequent amendments	Yes (on advice from treasury advisors)	Yes	These funds do not have a defined maturity date	25%	Yes

1. In determining the period to maturity of an investment, the investment should be regarded as commencing on the date of the commitment of the investment rather than the date on which funds are paid over to the counterparty
2. The use of the above instruments by the Council's fund managers will be by reference to the fund guidelines contained in the agreement between the Council and the Individual manager.
3. This currently covers the following:
   Building Societies with assets over £1bn: Max 364 days duration, max £5m limit per society.

Building Societies with assets of £500m-£999m: Max 6 months duration, max £3m limit
Building Societies with assets of £499 and under: Max 3 months duration, max £2m limit
Co-operative Bank: Max 364 days duration, max £5m limit.
Total investments in this category cannot exceed £25m

Appendix 4

INTRODUCTION:

The rules for Minimum Revenue Provision (MRP) were set out in the Local Authorities (Capital Finance and Accounting) (England) Regulations 2003. These rules have now been revised by the Local Authorities (Capital Finance and Accounting (England) (Amendment) Regulations 2008.

Authorities are required to submit to a meeting of their Council an annual statement of their policy on making MRP.

BACKGROUND:

Each year the Council borrows money in order to finance some of its capital expenditure. The loans taken out for this purpose, unlike a mortgage which is repaid in part each month, are fully repayable at a future point in time. The repayment date is chosen to secure the best financial result for the Council.

The concept of Minimum Revenue Provision was introduced in 1989 to prescribe a minimum amount which must be charged to the revenue account each year in order to make provision to meet the cost of repaying that borrowing.

The detailed rules and formulae to be used in the more recent method of calculation were laid down in the Regulations mentioned in the introduction section.

This system has now been radically revised and requires an annual statement to full Council setting out the method the authority intends to adopt for the calculation of MRP.

ISSUES AND/OR OPTIONS:

Under the old regulations Local Authorities were required to set aside each year, from their revenue account an amount that, in simple terms equalled approximately 4% of the amount of capital expenditure financed by borrowing. Local Authorities had no freedom to exercise any discretion over this requirement.

The amendment regulations introduce a simple duty for an authority each year to set aside an amount of MRP which it considers to be ‘prudent’. The regulation does not define a ‘prudent provision’ but the MRP guidance makes recommendations to authorities on the interpretation of that term.

The MRP guidance document is a statutory document and authorities are obliged by section 21 of the Local Government Act 2003 to have regard to such guidance. The guidance aims to provide more flexibility and in particular for development schemes it is possible to have an MRP “holiday” for assets or infrastructure under construction.

The operative date of the change was 31 March 2008, which means the new rules have applied since the financial year 2007/08.

The Annual MRP Statement

As stated above, Local Authorities are required under the new rules to prepare an annual statement of their policy on making MRP for submission to their full Council. This mirrors the existing requirements to report to the Council on the Prudential borrowing limit and investment policy. The aim is to give elected Members the opportunity to scrutinise the proposed use of the additional freedoms conferred under the new arrangements. The statement must be made before the start of each financial year.

The statement should indicate how it is proposed to discharge the duty to make prudent MRP in the financial year in question for the borrowing that is to take place in that financial year. If it is ever proposed to vary the terms of the original statement during any year, a revised statement should be put to Council at that time.

The guidance includes specific examples of options for making a prudent provision. The aim of this is to ensure that the provision to repay the borrowing is made over a period that bears some relation to the useful life of the assets in question.

Proposals

In 2013/14 it is proposed to continue with the regulatory method for supported borrowing and the asset life method for Prudential borrowing as in 2012/13. If this approach is agreed, the Minimum Revenue Provision Policy Statement for 2013/14 would be as follows:

- In accordance with the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 the Council's policy for the calculation of MRP in 2013/14 shall be the regulatory method for supported borrowing and the asset life (equal instalment) method for Prudential borrowing.

The policy will be reviewed on an annual basis.