21 February 2024	ITEM: 21
Cabinet	
Treasury Management – Mid-Year Report	
Wards and communities affected: All	**Key Decision:** Key
Report of: Steven Mair – Interim Chief Financial Officer/S151	
Accountable Assistant Director: Michael Jones – Interim Assistant Director for Strategic and Corporate Finance	
Accountable Director: Steven Mair – Interim Chief Financial Officer/S151	
This report is public	
Version: cabinet	

Executive Summary

The purpose of this report is to update Members on the delivery of the 2023/24 Treasury Management Strategy approved by Council on 1 March 2023.

One of the main financial issues facing the Council currently is the exceptionally high level of debt and the cost of this. One of DLUHC's key requirements is the reduction of this debt to a level that can be met within existing resources and enables the Council to become financially sustainable going forwards. This will take a number of years to achieve, however, the Council is pursuing measures that should enable a significant reduction to take place. These measures include, but are not limited to:

- disposal of capital investments and other assets
- a reduction in capital investment financed by borrowing,
- use of existing cash balances to finance capital purchases, and
- use of capital receipts to reduce outstanding debt.

Appendix 1 of this report sets out the performance of the Treasury Management function of the Council for the period 1 April to 30 September 2023. This includes:

- revisions to expected levels of external borrowing and the Council's Capital Financing Requirement as at 31 March 2024,
- revised assumptions in respect of asset disposals, disinvestments, and reductions to capital expenditure,
- current forecasts of investment income and interest charges for 2023/24, and
- the impact these will have on the expected outturn position at year-end.

Appendix 2 of the report provides a comparison of year-to-date and year-end forecasts for 2023/24 Prudential Indicators approved by members at the start of this financial year.

Appendix 3 sets out the proposed changes to the counterparty limits.

Commissioner Comment:

Commissioners support the recommendations as outlined in the report

1. Recommendation(s)

1.1 That Cabinet recommend to Full Council to agree the following amendment to the 2023/24 Treasury Management Strategy:

1. **That there is a revision to the Counterparty Limits in that investments placed with the Debt Management Office (DMO) are changed from £5m to unlimited.**

2. **Amend the Minimum Revenue Provision policy to revert back to Option 1 in respect of supported capital expenditure in line with the Statutory MRP Guidance.**

2. Introduction and Background

2.1 The Treasury Management Strategy sets out the Council's approach to ensuring cashflows are adequately planned to ensure that the capital programme and corporate investment plans are adequately funded, with cash being available when it is needed to discharge the Council's legal obligations and deliver Council services. It is also concerned with managing the debt position of the Council.

2.2 The original Treasury Management Strategy for 2023/24 was set by Full Council on 1 March 2023 (Decision: 110639). This strategy provided a delegation to officers to work within the approved parameters to deliver day-to-day Treasury Management functions and enable the requirements as set out above to be met.

2.3 The original report included assumptions about when receipts from sales and disinvestments would be received, the value of these and the impact this would have on the Council's borrowing levels going forwards. There were also assumptions related to wider economic issues, such as interest rates, and the Council's need to borrow going forwards.

2.4 Appendix 1 is the report on Treasury Management activities for the first half of the year and the projected year end position as at the mid-point in the current financial year.

3. Key Points and Changes to Assumptions

3.1 The fundamental elements that made up the original Treasury Management strategy for 2023/24 remain unchanged, namely that:

- A Debt Reduction Strategy is now in place,
- Going forward, new borrowing will be minimised,
- A Disinvestment Strategy is now in place to dispose of all non-cash investments and any assets held for operational purposes which are no longer required, and
- All proceeds of sale will be applied to reduce external debt.

3.2 The following points summarise the main changes to assumptions and estimations since the original strategy was approved in March 2023:

- Overall the Council's level of external borrowing has reduced by £100m from £1,553m as at 1 April 2023 to £1,453m as at 30 September 2023. This reflects a combination of improved cash management, disposal receipts and reductions in new borrowing for capital purposes,
- The timing of disposal proceeds expected from the sale of capital investments and other Council assets have been brought forward reflecting revised timings of expected sales.
- It is assumed that these receipts will be used in full to repay external borrowing, with appropriate reductions in interest charges and the Capital Financing Requirement.
- Going forward, proposed reductions to the capital programme should also reduce the Council's requirement for new borrowing between 2023/24 and 2025/26 from £152m to £58.7m.

3.3 Although there have been some changes to assumptions and estimations as set out above, as at 30 September 2023 the overall strategy and delegation arrangements set out in the original Treasury Management Strategy for 2023/24 continued to be sufficient for the day-to-day management of the Council's cash flows, disinvestment strategies and debt position. This will be supplemented by the proposed changes in section 5 below.

Investment performance monitoring

3.4 At over £1 billion, the value of investments is on the same level as for smaller local authority pension funds. The performance of local authority pension funds is heavily regulated to safeguard members' investments. Regulation includes:

- Setting performance benchmarks for assets classes over different time periods;
- Quarterly monitoring of investment performance for each investment;
- Provision of investment advice independent from the fund manager;
- Safeguarding of the assets by holding them through a custodian.

3.5 The Statutory Guidance on Local Government Investments does not explicitly specify an equivalent form of regulation, but nonetheless requires that authorities investing on non-specified investments should appropriate capacity, skills and information to enable both members and officers to make informed decisions about entering into and monitoring investments.

3.6 Historically, several of the key measures that would be expected of a local authority pension fund were not in place:

- no performance benchmarks have been set;
- for certain positions in the portfolio, there was not regular reporting in place to monitor the investments;
- there was not regular portfolio level monitoring, such as monitoring of risks and performance.

3.7 Action is now being taken to ensure that appropriate investment performance information is obtained for all investments, with the following reporting mechanisms being brought together/ in place:

- For the positions where divestment is in progress, such as Toucan, JLG/JCF and CCLA, regular meetings are held with the administrators and advisors on what are commercially sensitive matters. Nonetheless the Council did for the first time take a report to September Cabinet and Council and a further report on the fees aspect of this is elsewhere on this agenda. The Council has also prepared an extensive commercially confidential report to agree the sale of Toucan and which has now been made as public as possible and is also elsewhere on the agenda

- For the other positions in the portfolio over the past 6 months, the Council has contacted all investment counterparties to implement regular reporting and request additional information.

    - Where the Council's investment is in fund structures, such as the wind farms, quarterly reporting is being obtained from the fund managers. Several meetings have also been held with the managers, to explore options for divestment and to examine the performance of the fund.
    - For direct investments, there was typically annual reporting in place for the positions, but this was not submitted to Members. Alongside, the Council and its advisors have contacted all the counterparties and submitted information requests to obtain more detailed information. The information is being analysed, with option and/or briefing reports scheduled to be prepared over the next 2 months in order that from April 2024 the Cabinet and Council can be provided with performance monitoring information. There remains one position where information from the counterparty is not forthcoming, the Council is currently seeking to obtain further information.

3.8 The Council holds a weekly meeting with its advisors to assess key next steps, ultimately, with the objective of optimising returns to the Council and mitigating risks. The focus has been on the largest portfolio positions to date, comprising more than 90% of the total portfolio value. There are also regular meetings held on specific workstreams, such as potential litigation

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4. Issues, Options and Analysis of Options

4.1 This report reflects the factual position in respect of debt and treasury management for the first half of the 2023/24 financial year. Key assumptions and estimations that have been used to forecast the year end position are based on the information available at the time of preparation of this report and a prudent view has been taken.

4.2 These assumptions will continue to be reappraised and any necessary amendments will be included in the 2024/25 Treasury Management Strategy and 2023/24 Treasury Management year-end report.

5. Reasons for Recommendation

5.1 Under the requirements of the Treasury Management Code, the Council is required to have a mid-year Treasury Management report agreed by Full Council. This report to the Corporate Overview and Scrutiny Committee and Cabinet is, therefore, the first step in this process.

Counterparty limits

5.3 Full Council will be asked to approve a change to the original Treasury Management Strategy in respect of Counterparty Limits. The table from the original strategy is included as Appendix 3, which shows a £5m limit on investments than can be placed with another Local Authority, or with the Debt Management Office (DMO). The DMO is a government agency (part of HM Treasury) that provides loans to local authorities (and others) through the Public Works Loans Board (PWLB) and an investment facility for surplus cash. The DMO will always accept any surplus cash from any local authority and will pay a yield, in the form of interest, on any deposits while held by them.

5.4 As it is part of government, it is highly secure and as they are not limited on sums taken, is often used as an alternative if cash cannot be placed with any other counterparty.

5.5 During 2023/24, the £5m limit on the DMO facility was breached 52 times. It also utilised Link which resulted in a further 57 breaches being a mix of sums exceeding approved limits, inadequate credit rating and foreign domicile. This practise has now ended. In addition, the Council is likely to be in a position over the coming months when large cash deposits are received from sales and disinvestments and this change in policy will allow for officers to ensure that cash received is kept securely until such time as it is required for the repayment of debt. It should be noted that it is not uncommon for a local authority to have an unlimited limit with the DMO to assist with the management of cash flows and it is likely that, if approved, this will remain in place for future years. In particular, it is anticipated that the Council will receive about £600m in asset sale receipts before the end of the financial year and thus will breach the current DMO limit. Approval by the Council of the recommendation to increase the limit will regularise this breach.

MRP Policy Statement

5.6 The MRP Policy Statement forms part of the annual budget setting framework. Paragraph 10 of Annex B to the 2018 Statutory MRP Guidance explains that the purpose of preparing a MRP

Statement "*is to give elected Members the opportunity to scrutinise the proposed use of the additional freedoms conferred under the new arrangements*".

5.7 When reporting its proposed MRP policy for the forthcoming year, the Council must therefore both demonstrate that the authority has had regard to the Statutory MRP Guidance and also provide sufficient detailed information to allow elected members to make an informed decision. About whether or not to approve the proposed policy. Therefore, the proposed policy should explain:

- What the four suggested calculation options are under the Statutory MRP Guidance;
- Whether there are any proposed deviations from these four options; and
- Where any deviations are proposed, an explanation of how, and confirmation that, the proposed policy still provides a "prudent" level of MRP.

5.8 Prior to 2023/24, none of the MRP Policy Statements provided the above information to elected Members, so provided insufficient information for Members to make an informed decision.

5.9 The following changes were made to the Council's MRP calculations:

- In 2016/17 the MRP policy was amended in respect of supported capital expenditure[1] to charge MRP on a straight-line over a 50 year period and was backdated to 1 April 2008. There was no mention that this was a deviation from the Statutory MRP Guidance which only permits the use of Options 1 or 2 to be used to calculate MRP for supported capital expenditure.
- In 2017/18, the calculation of the MRP on supported capital expenditure was further amended to an annuity method. The impact of using an annuity approach was to shift the incidence of the MRP charge into future years which is in direct opposition to the reducing balance method of Options 1 and 2. The change in method was not reported to Members.

5.10 Discussions with DLUHC and CIPFA have confirmed that only Options 1 and 2 are permissible methods for calculating MRP on supported capital expenditure.

5.11 Notwithstanding that the MRP policies which the Council had approved in previous years did not follow the statutory MRP Guidance, legal advice obtained confirms that the MRP policies in those years were properly approved in line with the Council's decision-making processes and thus lawfully set.

5.12 Therefore to bring the MRP policy in line with the MRP Guidance, the MRP policy is to be changed with effect from 1 April 2023 as reported in this report. This reduces the Capitalisation Direction (CD) for 2022/23 by £412m to £40m by eliminating the entries for corrections to MRP understated when compared with the MRP Guidance, and thus the MRP on the CD for 2023/24 reduces to £1.3m in 2023/24. However, the impact of changing the MRP with effect from 1 April 2023 is that where MRP had not been charged on the investment asset portfolio from inception, MRP has to be calculated over the residual lives of the investment assets at 31 March 2023. This increases the MRP charge for 2023/24 by £55m to £235m.

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[1] Prior 1 April 2011, an element of revenue support grant was to support borrowing for capital projects. This was known as "supported capital expenditure".

6. Consultation (including Overview and Scrutiny, if applicable)

6.1 This report has been reviewed by the Senior Management Team and by the Commissioners. The Corporate Overview and Scrutiny Committee can comment on the report prior to submission to Cabinet and Full Council.

7. Impact on corporate policies, priorities, performance and community impact

7.1 The issues identified in this report have driven DLUHC intervention at the Authority, the issuing of a Section 114 Notice and Directions from the Secretary of State. This will fundamentally impact on how services are delivered in Thurrock and changes to Treasury Management practices form part of the delivery of the Council's wider improvement and recovery plan.

8. Implications

8.1 **Financial**

Implications verified by: **Michael Jones**

Interim Assistant Director for Strategic and Corporate Finance

The financial implications are set out in the body of the report.

8.2 **Legal**

Implications verified by: **Mark Bowen**

Interim Project Lead - Legal

The report provides an update to members as required by the Treasury Management Code and there are no specific legal implications arising from the report.

8.3 **Diversity and Equality**

Implications verified by: **Rebecca Lee**

Team Manager, Community Development and Equalities

There are no specific diversity and equality implications to note from the report.

8.4 **Risks**

8.5 **Other implications** (where significant) – i.e. Staff, Health Inequalities, Sustainability, Crime and Disorder, or Impact on Looked After Children

None

9. Background papers used in preparing the report (including their location on the Council's website or identification whether any are exempt or protected by copyright):

10. Appendices to the report

- Appendix 1 – Treasury Management Interim Report
- Appendix 2 – Key Prudential Indicators 2023/24
- Appendix 3 – Changes to Approved Counterparty Limits from Original 2023/24 Treasury Management Strategy

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