REPORT TO:	**FINANCE AND MANAGEMENT COMMITTEE**	**AGENDA ITEM: 8**
DATE OF MEETING:	**19th FEBRUARY 2015**	**CATEGORY: RECOMMENDED**
REPORT FROM:	**DIRECTOR OF FINANCE and CORPORATE SERVICES**	**OPEN**
MEMBERS' CONTACT POINT:	**KEVIN STACKHOUSE (01283 595811)** **Kevin.stackhouse@south-derbys.gov.uk**	**DOC:** u/ks/treasury management/strategies/strategy 2015-16
SUBJECT:	**TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL INDICATORS 2015/16**	**REF:**
WARD(S) AFFECTED:	**ALL**	**TERMS OF REFERENCE: FM 08**

1.0 Recommendations

1.1 That the Treasury Management Strategy for 2015/16 is approved.

1.2 That the Prudential Indicators and Limits for 2015/16 to 2019/20 as set out in **Appendix 1** are approved.

1.3 That the Investment Strategy for 2015/16 including the associated counterparty (lending) list and policy is approved.

1.4 That the Council becomes a corporate member of the South Derbyshire Credit Union with an investment of £10,000.

1.5 That a further sum of £40,000 is made available to the Credit Union as an interest free loan and is subject to an annual review.

2.0 Purpose of the Report

2.1 To detail the Council's Prudential Indicators for its expected treasury operations for 2015/16. This is in accordance with the requirements of the Local Government Act 2003, updated for matters arising out of the Localism Act 2011. Three main areas are covered:

- The CIPFA Prudential Code (2011) requires the reporting of the Indicators for Capital Finance in Local Authorities.
- The Treasury Strategy in accordance with the CIPFA Code of Practice on Treasury Management.
- The Investment Strategy in accordance with Government guidance (2010).

2.2 The report also proposes financial support to the South Derbyshire Credit Union. This follows a resolution at the Full Council meeting in January 2014 (CL/63) which asked the Council to consider the practicalities of making an interest free loan of £50,000 to the Credit Union.

3.0 Executive Summary

The Prudential System for Capital Finance

3.1 The main aims of the national prudential system are to ensure that:

- Capital investment plans of local authorities are affordable and sustainable.

- Treasury management decisions are taken in accordance with best professional practice.

- Financial planning and asset management are integrated into the Council's overall corporate planning arrangements.

3.2 Treasury operations are measured within a set of prudential indicators. The main purpose of these indicators is to provide the limits and benchmarks to control the level of capital expenditure, borrowing and investment. The Council is expected to operate comfortably within these limits.

3.3 The Prudential System allows councils the freedom to borrow on a prudential basis. Any new borrowing has to be accommodated within any maximum debt limits or caps set by the Government and the Council has to demonstrate that it can afford to service and repay the debt within its financial plan.

The Treasury Management Strategy

3.4 The Strategy aims to provide transparency for treasury decisions including the use of counterparties, together with assessing how risk is managed on a day to day basis.

Prudential Indicators

3.5 The relevant indicators required under the regulations are summarised in the following sections.

Estimated Capital Expenditure

3.6 This is the approved capital investment programme for the General Fund, together with stock investment proposals included in the HRA Business Plan. The programme is summarised in the following table.

Estimated Capital Expenditure	2014/15 £	2015/16 £	2016/17 £	2017/18 £	2018/19 £	2019/20 £
General Fund	2,558,673	5,742,600	548,404	592,285	478,731	504,580
HRA	5,812,000	11,031,000	10,295,000	5,943,000	6,092,000	4,595,000
TOTAL	**8,370,673**	**16,773,600**	**10,843,404**	**6,535,285**	**6,570,731**	**5,099,580**

3.7 The capital expenditure programme will be financed mainly from government grants, external contributions, council reserves and capital receipts. Some external borrowing may be undertaken in 2016/17 depending upon further phases of the Council's New Build Programme for Council Housing.

Capital Financing Requirement (CFR) and Debt Outstanding

3.8 The CFR is a measure of the Council's underlying need to borrow for capital investment. It is based on the value of its assets contained in the Balance Sheet.

3.9 The CFR does not necessarily represent the amount of actual external debt outstanding. This is due to the fact that not all borrowing previously allowed has in effect taken place against this requirement, but is being financed internally through cash deposits and reserves.

Debt Pools

3.10 The Council operates two separate Debt Pools for the General Fund and the Housing Revenue Account (HRA). There is no external debt currently outstanding on the General Fund, although it has a positive CFR representing an underlying borrowing need.

3.11 The General Fund CFR is reduced each year by a statutory revenue charge known as the Minimum Revenue Provision (MRP). In addition a Voluntary Revenue Provision (VRP) is made where borrowing has taken place on a prudential basis.

3.12 There is no requirement to make a MRP or VRP in the Housing Revenue Account. The HRA has debt outstanding of just over £57m. This represents the debt take-on under the self-financing framework for Council Housing.

3.13 Although no MRP is made, in future years, money will be set-aside to repay the HRA debt in accordance with the maturity profile. This strategy is reflected in the HRA's Business Plan.

3.14 The expected CFRs over the current financial planning period to 2020 are detailed in the following table.

Expected CFRs	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
General Fund	6,540	6,375	6,020	5,673	5,335	5,005
HRA	61,583	61,583	61,583	61,583	61,583	61,583
TOTAL	**68,123**	**67,958**	**67,603**	**67,256**	**66,918**	**66,588**

3.15 The CFR on the General Fund will continue to reduce over the medium-term due to MRP/VRP. These charges, which are £352,000 in 2014/15 and £365,000 in 2015/16, are included in the Council's base budget.

3.16 The CFR in 2015/16 allows internal borrowing of £200,000 to finance the Grove Hall Extreme Sports Development project (as previously approved by the Committee).

3.17 Effectively, the MRP/VRP creates a cash amount in the Council's budget in order to write down the underlying borrowing requirement. The larger CFR on the HRA is forecast to remain static until such time as any new borrowing is undertaken or until the first repayment of self-financing debt in 2022.

Operational Boundaries and Limits

3.18 These are summarised in the following table.

Debt Limits	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
Authorised Limit - General Fund	6,540	6,375	6,020	5,673	5,335	5,005
Authorised Limit - HRA	66,853	66,853	66,853	66,853	66,853	66,853
Operational Boundary	62,423	62,423	62,423	62,423	62,423	62,423

3.19 The Authorised Limit is the borrowing cap for the Council. It includes the CFR on the General Fund, plus the debt cap set by the Government on the HRA for self-financing, i.e. £66.853m. The Operational Boundary represents the expected fixed external debt outstanding in the year (HRA at £57.423m) plus a provision for temporary borrowing of £5m.

Cost of Debt to Finance Capital Expenditure

3.20 The estimated cost of debt, to finance the capital programme contained in the consolidated budget proposals on Council Tax and Housing Rents are summarised in the following table.

Cost of Servicing Debt (per year)	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Band D Council Tax	-£1.30	-£0.94	-£1.46	-£2.13	-£1.94	-£1.92
Per Council Dwelling	£623	£552	£656	£686	£719	£728

3.21 As there is no actual debt on the General Fund, the impact on Council Tax is positive as this represents interest on cash deposits. The surplus is expected to rise moderately in the medium term in accordance with interest rates.

Available Resources for Investment

3.22 This represents balances and reserves held for specific purposes and to act as a contingency / provision. These are the resources the Council has to invest and to internally finance any short term borrowing requirement. The estimated year end position is shown in the following table.

Estimated Resources Available	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
TOTAL	**15,797**	**16,145**	**12,561**	**13,748**	**15,414**	**16,666**

3.23 The table shows that overall the level of resources is estimated to increase. This is due to resources being set-aside in the HRA to repay debt.

3.24 Base on this level of reserves, it is estimated that the Council will physically have an amount of at least £7m invested at each year end. In accordance with the Investment Strategy, this will continue to be held in short-term (less than 364 days) deposit accounts.

4.0 <u>Detail</u>

Prudential Indicators for Capital Expenditure and Borrowing

4.1 The Local Government Act 2003 requires the Council to adopt the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code and in doing so, to calculate and monitor a set of prudential indicators. The Code and indicators should sit alongside the Council's main financial plan.

4.2 The prudential framework is designed to control the level of borrowing and investment activity at a local level. The indicators themselves either summarise the expected treasury activity or place limits upon the activity that reflect the outcome of the Council's underlying capital expenditure and borrowing requirements.

4.3 A fundamental part of the Code is the requirement to adopt and utilise a Treasury Management Strategy. The Council's proposed strategy for 2015/16 is detailed in **Appendix 2.** The Prudential Indicators are detailed in **Appendix 1** with comments and analysis in the following sections.

Capital Expenditure and Financing

4.4 The approved capital programme is summarised in the following table.

Estimated Capital Expenditure	2014/15 £	2015/16 £	2016/17 £	2017/18 £	2018/19 £	2019/20 £
General Fund	2,558,673	5,742,600	548,404	592,285	478,731	504,580
HRA	5,812,000	11,031,000	10,295,000	5,943,000	6,092,000	4,595,000
TOTAL	**8,370,673**	**16,773,600**	**10,843,404**	**6,535,285**	**6,570,731**	**5,099,580**
Financed By						
Grants	1,448,143	1,548,637	456,000	446,000	446,000	446,000
Major Repairs Reserve	943,000	6,670,000	1,800,000	2,686,000	2,679,000	402,000
External / Partnership	134,394	771,076	0	0	0	0
Revenue Contributions	4,270,320	3,745,000	2,705,000	2,842,000	3,063,000	3,105,000
Earmarked Reserves	913,920	2,556,174	445,404	499,285	382,731	409,580
Capital Reserves	476,897	980,713	0	0	0	0
Loan	0	0	5,375,000	0	0	737,000
General Reserve	183,999	477,000	62,000	62,000	0	0
Sinking fund	0	25,000	0	0	0	0
TOTAL	**8,370,673**	**16,773,600**	**10,843,404**	**6,535,285**	**6,570,731**	**5,099,580**

4.5 The table highlights that the 5-year investment programme is fully funded. There is no requirement to enter into any new external borrowing, i.e. there is no additional net financing requirement, subject to the HRA New Build Programme (see below).

4.6 If all financing is not secured, expenditure can be curtailed or other resources and reserves identified. Due to the current level of reserves and cash on deposit, current policy is that any longer term borrowing is undertaken as a last resort to meet any shortfall; any new borrowing is undertaken prudentially within the Council's debt limit.

HRA New Build

4.7 As stated above, it is not expected that any additional borrowing will be required over the financial planning period. However, the HRA Business Plan does allow for additional borrowing up to the HRA's debt cap. This would allow a further £9.5m to finance New Build.

4.8 The full implications of future New Build programmes beyond the initial 1st phase are still subject to an options appraisal. This is unlikely to occur in 2015/16 and future treasury management considerations associated with New Build will form part of the options appraisal.

The Council's Borrowing Need or Capital Financing Requirement (CFR)

4.9 The CFR is a measure of the Council's underlying need to borrow for capital investment and is based on the net value of its assets contained in the Council's Balance Sheet.

4.10 Capital expenditure that has not been immediately paid for increases the CFR through additional borrowing. The CFR is reduced following debt repayment or through setting-aside revenue sums to repay internal borrowing.

4.11 The Council is required to pay off an element of the accumulated General Fund CFR each year through a revenue charge called the Minimum Revenue Provision (MRP). In addition a Voluntary Revenue Provision (VRP) is made where borrowing has taken place on a prudential basis.

4.12 There is no requirement to make a MRP for the HRA. However, in future years, money will be set-aside to repay HRA debt in accordance with the maturity profile. This strategy is reflected in the HRA's Business Plan.

4.13 A summary of the CFR estimates is shown in the following table.

Expected CFRs	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
CFR b/fwd	69,475	68,123	67,958	67,603	67,256	66,918
Add Net Financing	0	200	0	0	0	0
Less MRP	-242	-233	-223	-215	-206	-198
Less VRP	-110	-132	-132	-132	-132	-132
Less Loan Repayments	-1,000	0	0	0	0	0
CFR c/fwd	**68,123**	**67,958**	**67,603**	**67,256**	**66,918**	**66,588**
General Fund Proportion	6,540	6,375	6,020	5,673	5,335	5,005
HRA Proportion	61,583	61,583	61,583	61,583	61,583	61,583

4.14 The Committee has previously approved the use of prudential borrowing from internal reserves as part of the funding package to redevelop the Grove Hall in Swadlincote. Therefore, provision of £200,000 has been made in 2015/16 as new financing.

4.15 The VRP relates to the repayment of previous internal borrowing relating to the purchase of receptacles to extend the kerbside recycling scheme in 2013, together with the repayment of the internal borrowing for the Grove Hall project.

4.16 The HRA CFR is projected to remain static over the current financial planning period, subject to any new borrowing undertaken as highlighted previously.

4.17 The loan repayment of £1m shown in the previous table, relates to the repayment of a remaining market loan. This was repaid in October 2014 as reported to the Committee in December. It was repaid in accordance with the current Treasury Management Strategy for 2014/15.

The Use of the Council's Resources and the Investment Position

4.18 The Council has available at any one time, reserves and balances which are held to finance future expenditure commitments or to act as a contingency sum as recommended by the Council's Chief Finance Officer.

4.19 These balances are available for investment on a short-term basis in accordance with the Investment Strategy. The expected level of reserves and balances is shown in the following table.

Usable Reserves	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
General Fund	5,858	5,068	4,733	4,117	3,281	2,160
Earmarked Reserves	3,410	3,332	1,818	1,768	2,093	2,118
HRA	1,100	1,400	1,200	3,600	6,000	9,300
Capital Receipts	5,429	6,345	4,810	4,263	4,040	3,088
TOTAL	**15,797**	**16,145**	**12,561**	**13,748**	**15,414**	**16,666**

4.20 The table shows that overall the level of resources is estimated to increase. This is due to resources being set-aside in the HRA to repay debt. Other reserves show an incremental drawdown as planned expenditure is incurred.

4.21 Based on this level of reserves, it is estimated that the Council will physically have an amount of at least £7m invested at each year end. In accordance with the Investment Strategy, this will continue to be held in short-term (less than 364 days) deposit accounts.

Limits to Borrowing Activity

4.22 The Council is required to set limits on overall borrowing (net of investments). This controls borrowing and ensures that it does not, except in the short term, exceed the total of the CFR in the preceding year, plus the estimates of any additional CFR for the current and the next two financial years.

4.23 A short term deviation is allowed for flexibility if a limited amount of borrowing was required to meet temporary shortfalls in cash flow. The estimated position is detailed in the following table.

Estimated Borrowing Compared to the CFR	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
Gross Borrowing - HRA	57,423	57,423	57,423	57,423	57,423	57,423
Gross Borrowing - General Fund	27	27	27	27	27	27
Gross Borrowing - Total	**57,450**	**57,450**	**57,450**	**57,450**	**57,450**	**57,450**
Total CFR	**68,123**	**67,958**	**67,603**	**67,256**	**66,918**	**66,588**

4.24 The above table shows that as gross borrowing is likely to remain below the CFR, the Council will comply with this Prudential Indicator.

4.25 The small level of debt on the General Fund relates to deposits held on account for Parish Councils and these are subject to repayment at short notice. The figures show the estimated year-end position and do not take into account any short-term cash deposits which could offset the CFR.

4.26 The Council's overall financial plans do not at this stage rely on any further new borrowing whether on a prudential or unsupported basis. As previously highlighted, the position on the HRA Business Plan will be kept under review.

The Authorised Limit for External Debt

4.27 This represents a limit beyond which external debt is prohibited. It is the statutory limit determined under section 3(1) of the Local Government Act 2003 and includes the debt cap for HRA self-financing of £66.853m.

The Operational Boundary for External Debt

4.28 This represents the expected external debt during the course of the year, but it is not a limit. It is designed to aid the Director of Finance to manage treasury activity on a daily basis and acts as an early warning sign of any potential issues. It includes a provision for temporary borrowing of £5m. The Limit and Boundary are summarised in the following table.

Debt Limits	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
Authorised Limit - General Fund	6,540	6,375	6,020	5,673	5,335	5,005
Authorised Limit - HRA	66,853	66,853	66,853	66,853	66,853	66,853
Operational Boundary	62,423	62,423	62,423	62,423	62,423	62,423

Affordability Indicators

4.29 These indicators show the cost of borrowing and capital investment plans on the Council's finances, together with their impact on local taxpayers. Under the Prudential System, borrowing needs to be affordable and sustainable in the longer term.

Ratio of Financing Costs to Net Revenue Stream

4.30 This indicator shows the trend in the net cost of borrowing (allowing for investment income) against the net revenue stream, i.e. Council Tax for the General Fund and Rent Income for the HRA. Estimates included the Council's Medium Term Financial Plan (MTFP) are shown in the following table.

Financing Ratios	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
General Fund						
Council Tax Income	£4,465,881	£4,598,852	£4,736,806	£4,878,438	£5,023,840	£5,173,108
Net Interest	-£38,517	-£28,833	-£45,175	-£66,425	-£61,000	-£61,000
Proportion	-0.86%	-0.63%	-0.95%	-1.36%	-1.21%	-1.18%
HRA						
Rent Income	12,390,000	12,591,000	13,131,000	13,658,000	14,038,000	14,420,000
Net Interest	£1,861,000	£1,669,000	£2,006,000	£2,094,000	£2,186,000	£2,204,000
Proportion	15.02%	13.26%	15.28%	15.33%	15.57%	15.28%

4.31 With no debt on the General Fund, the indicator is negative. The ratio reflects the level of "gearing" - how much of the Council's revenue is tied up in borrowing costs. Although the proportion for the HRA is greater in percentage terms, this is a relatively fixed cost and affordable within the Business Plan.

Impact of Capital Investment on the Council Tax and Housing Rents

4.32 This indicator shows how much per year the costs of borrowing impact upon each household (at Band D Council Tax rate) in the District and for each council tenant (HRA).

Cost of Servicing Debt	2014/15	2015/16	2016/17	2017/18	2018/19	2019/20
Net Interest Received - Gen Fund	-£38,517	-£28,833	-£45,175	-£66,425	-£61,000	-£61,000
Estimated Band D Properties (per MTFP)	29,723	30,608	30,908	31,208	31,508	31,808
Cost per Band D Property	**-£1.30**	**-£0.94**	**-£1.46**	**-£2.13**	**-£1.94**	**-£1.92**
Estimated Interest - HRA	£1,861,000	£1,669,000	£2,006,000	£2,094,000	£2,186,000	£2,204,000
Estimated Dwellings	2,989	3,024	3,059	3,054	3,041	3,028
Annual Cost per Dwelling	**£623**	**£552**	**£656**	**£686**	**£719**	**£728**

Other Treasury Matters – Credit Union Loan

4.33 In January 2014, the Council resolved to support the local South Derbyshire Money Spider Credit Union with an interest free loan of £50,000. This was in recognition of:

- "*A legitimate consumer demand among the communities of South Derbyshire for short-term loan facilities*.
- *A concern with the growth of heavily marketed payday lending companies which can allow financially challenged borrowers into unsustainable debt*.

- *Encouraging increased access to not-for-profit credit unions including specifically Money Spider*. “

4.34 Consequently, liaison took place with the Money Spider Credit Union that covers South Derbyshire and East Staffordshire, based in Swadlincote. In accordance with the Council resolution, this examined the practicalities of £50,000 being made available through the Credit Union for subsequent lending (through loans) to help eligible local residents.

4.35 However, due to the framework in which the Credit Union is structured and regulated through the Financial Conduct and the Prudential Regulation Authorities, this is not practical.

4.36 The amount involved and the need to eventually repay the loan back to the Council, would not meet a key financial ratio (assets to liabilities) that governs the financing of the Credit Union.

4.37 Unless the Council gave a direct grant or financial contribution to the Credit Union without the requirement to repay it back, there does not appear to be a ready method available, which would satisfy the Regulators, for the Credit Union to make this money available for loans.

4.38 Therefore, alternative methods of making an amount of £50,000 available to the Credit Union, in the form of an interest free loan, in order for them to benefit in some other way have been considered.

4.39 Consequently, the proposal is still to provide an interest free loan, but this would provide working capital for the Credit Union as follows:

- £10,000 would enable the Council to become a corporate member of the Credit Union. Up to 70% of this amount would be available for the Credit Union to recycle in the form of loans to the local community. This amount and arrangement would satisfy the Regulator.

- £40,000 would be directly invested by the Credit Union into a 1-year interest earning bond. The Credit Union would be able to take advantage of favorable terms, with the return on this money enabling the Credit Union to meet day to day expenses and ease the burden of running costs.

4.40 The amount of £10,000 would effectively be a deposit which could be recalled at any time. However, to enable the Credit Union to have some certainty, it is recommended that the total loan is reviewed on an annual basis. This would also allow the Credit Union to enter into a fixed rate bond (with the £40,000) to achieve the best possible rate of return.

Legal Basis

4.41 The Council has the power to enter into this arrangement by virtue of the Localism Act 2011 and in particular the General Power of Competence contained in Section 1.

4.42 Under this provision, a local authority has power to do anything that individuals of full legal capacity may do, to give authorities the power to take reasonable action they need "*for the benefit of the authority, its area or persons resident or present in its area*."

The Potential Costs and Risk

4.43 The cost to the Council would effectively be the loss of interest on the principal amount lent of £50,000. This is considered neglible at a current interest rate of 0.5%, the loss of interest equates to approximately £250 per year.

4.44 The element of £10,000 would attract an annual dividend payable to the Council. In recent years, this has been between 0.5% and 0.75%.

4.45 The Investment Bond proposed by the Credit Union for the £40,000 element is protected by the Government's Deposit Guarantee Scheme which provides cover of up to £85,000 should the counterparty default.

4.46 In addition, the £10,000 element is also protected through the same scheme.

4.47 The principal amount would not be a charge on the revenue of the Council and can easily be accommodated from the Council's reserve and cash balances. Effectively, it would be carried as a short-term investment on the Council's Balance Sheet.

5.0 Financial Implications

5.1 As detailed in the report.

6.0 Corporate Implications

6.1. None directly

7.0 Community Implications

7.1 None directly

8.0 Background Papers

8.1 Treasury Management in Public Services and the Code of Practice (Cipfa Publication – November 2011)

8.2 Local Government Act 2003 (Part 1)

8.3 Localism Act 2011 – Part 7 Chapter 3

Appendix1: LIST OF PRUDENTIAL INDICATORS 2014/15 to 2019/20

External Debt	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
Debt 1st April	58,457	57,450	57,450	57,450	57,450	57,450
New Debt	0	0	0	0	0	0
Maturing Debt	-1,007	0	0	0	0	0
Debt 31st March	**57,450**	**57,450**	**57,450**	**57,450**	**57,450**	**57,450**
Annual Change in Debt	-1,007	0	0	0	0	0
Long-term Investments	0	0	0	0	0	0
Short-term Investments	7,456	6,456	5,456	4,456	3,456	2,456

Limits compared to Actual Debt	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
Authorised Limit - General Fund	6,540	6,375	6,020	5,673	5,335	5,005
Authorised Limit - HRA	66,853	66,853	66,853	66,853	66,853	66,853
Financing Requirement	68,123	67,958	67,603	67,256	66,918	66,588
Operational Boundary	62,423	62,423	62,423	62,423	62,423	62,423
Gross Debt	57,450	57,450	57,450	57,450	57,450	57,450
Debt Less Investments	49,994	50,994	51,994	52,994	53,994	54,994

General Fund - Net Indebtedness	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
CFR	6,540	6,375	6,020	5,673	5,335	5,005
Estimated Reserves	9,268	8,400	6,551	5,885	5,374	4,278
Net Indebtedness	**-2,728**	**-2,025**	**-531**	**-212**	**-39**	**727**

HRA Limit on Indebtedness	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
HRA Debt Cap	66,853	66,853	66,853	66,853	66,853	66,853
HRA CFR	61,583	61,583	61,583	61,583	61,583	61,583
Difference	5,270	5,270	5,270	5,270	5,270	5,270
HRA Debt	57,423	57,423	57,423	57,423	57,423	57,423
Borrowing Headroom	**9,430**	**9,430**	**9,430**	**9,430**	**9,430**	**9,430**

Interest Payable and Receivable	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
General Fund						
Interest Payable	4	4	4	4	4	4
Interest Received	-49	-39	-58	-83	-86	-86
HRA						
Interest Payable	1,874	1,685	2,020	2,120	2,222	2,269
Interest Received	-13	-16	-14	-26	-36	-65

Appendix 2

South
Derbyshire
District Council

Treasury Management and Investment Strategy 2015/16

February 2015

1.0 Introduction

1.1 The treasury management service is an important part of the overall financial management of the Council's affairs. Supplemented by a series of Prudential Indicators, this helps to consider the affordability and impact of capital expenditure decisions, together with the associated borrowing and investment.

1.2 The treasury service considers the effective funding of these decisions. It forms part of the process that ensures the Council achieves a balanced budget requirement under the Local Government Finance Act 1992.

1.3 The Council's treasury activities are regulated by statutory requirements and a professional code of practice (the CIPFA Code of Practice on Treasury Management).

1.4 The Council has adopted the Code and as a result, has adopted a Treasury Management Policy Statement.

Reporting Treasury Management

1.5 A key requirement of this report is to explain both the risks, and the management of the risks, associated with the treasury service. Updates on treasury activity are reported to the Finance and Management Committee on a quarterly basis.

1.6 A further treasury report is produced alongside the final accounts each June to detail all activity for the year.

Responsibility for Treasury Management

1.7 The Finance and Management Committee is responsible for setting and monitoring treasury activity at the Council. Under its terms of reference, this includes ensuring that the Council does not breach its borrowing limit.

1.8 The Committee is advised by its Section 151 (Chief Finance) Officer who is the Director of Finance and Corporate Services. This Officer is responsible for the oversight of activity and to ensure that treasury strategy and associated policies are met.

1.9 The day to day operational activity is undertaken within the Financial Services Unit at the Council. The main officers who have responsibility for daily transactions are the Financial Accountant and Finance Services Officer.

1.10 The Authorising Officers for transactions are the Director of Finance, Financial Services Manager and the Client Services Officer. Any new borrowing or investment has to have the prior approval of the Director of Finance.

External Support for Treasury Activity

1.11 All designated officers involved in treasury activity are covered under the Council's insurance. Officers are also supported by external treasury advisors who provide research material, news bulletins, together with general advice and guidance.

Audit Arrangements

1.12 The Council's Internal Audit function audits treasury policies and procedures, together with treasury activity and transactions at least once per year. This is a requirement of External Audit. Any matters raised are considered and monitored by the Council's Audit Sub Committee.

The Strategy

1.13 This strategy covers:

- The management of debt
- The Council's debt and investment projections.
- The expected movement in interest rates.
- The Council's borrowing and investment strategies.
- Treasury performance indicators.
- Specific limits on treasury activities.
- Any local treasury issues.

2.0 Debt and Investment Projections

2.1 The table below shows the expected debt position of the Council over the Medium Term Financial Planning (MTFP) period.

External Debt	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
Debt 1st April	58,457	57,450	57,450	57,450	57,450	57,450
New Debt	0	0	0	0	0	0
Maturing Debt	-1,007	0	0	0	0	0
Debt 31st March	**57,450**	**57,450**	**57,450**	**57,450**	**57,450**	**57,450**
Annual Change in Debt	-1,007	0	0	0	0	0
Long-term Investments	0	0	0	0	0	0
Short-term Investments	7,456	6,456	5,456	4,456	3,456	2,456

2.2 A comparison of this estimated debt position with the various borrowing limits is shown below.

Limits compared to Actual Debt	**2014/15 £'000**	**2015/16 £'000**	**2016/17 £'000**	**2017/18 £'000**	**2018/19 £'000**	**2019/20 £'000**
Authorised Limit - General Fund	6,540	6,375	6,020	5,673	5,335	5,005
Authorised Limit - HRA	66,853	66,853	66,853	66,853	66,853	66,853
Financing Requirement	68,123	67,958	67,603	67,256	66,918	66,588
Operational Boundary	62,423	62,423	62,423	62,423	62,423	62,423
Gross Debt	57,450	57,450	57,450	57,450	57,450	57,450
Debt Less Investments	49,994	50,994	51,994	52,994	53,994	54,994

2.3 The above table shows that debt outstanding is expected to be comfortably below the Financing or underlying Borrowing Requirement (CFR) and well within the Authorised Limit (Debt Cap).

2.4 The Operational Boundary allows a temporary borrowing requirement of £5m. However, it is expected that the Council will continue to be a net lender of funds on a day to day basis.

Management of Debt

2.5 As approved by the Finance and Management Committee on 23rd January 2012, the Council decided to adopt a “two pool” approach to debt management. This involves splitting borrowing between the General Fund and the HRA and then allocating new loans to each pool as required.

2.6 This has been adopted for clarity and transparency and ensured there was no detriment to the General Fund on transition to HRA self-financing in 2012. Treasury Management decisions on the structure and timing of borrowing are made independently for the General Fund and HRA.

2.7 Interest on loans is calculated in accordance with proper accounting practice and allocated to either pool accordingly.

2.8 It is not anticipated that there will be a requirement to transfer loans between the two pools. Any proposals to do this will be need to be considered and approved separately.

Internal Borrowing – Cash Management

2.9 Both the HRA and General Fund are likely to have surplus cash balances which will allow either account to have external borrowing below its Capital Financing Requirement.

2.10 The interest earned on all investments is initially allocated to the General Fund with a proportion allocated to the HRA based on the average rate of interest earned on the average cash balances during the year.

Use of Financial Instruments

2.11 The Council does not use any type of derivative instruments, such as interest rate swaps or hedge accounting, to manage the risk of borrowing.

General Fund Debt

2.12 The General Fund does not currently have any actual debt outstanding and its underlying borrowing requirement is financed from reserves and balances as shown in the following table.

General Fund - Net Indebtedness	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
CFR	6,540	6,375	6,020	5,673	5,335	5,005
Estimated Reserves	9,268	8,400	6,551	5,885	5,374	4,278
Net Indebtedness	**-2,728**	**-2,025**	**-531**	**-212**	**-39**	**727**

2.13 However, the table also shows that by 2019/20, the underlying indebtedness increases to a position where borrowing may apply. This will depend on overall cash flow and this is likely to be a temporary position. However, it will be kept under review.

HRA and Limit on Indebtedness

2.14 Under self-financing, the HRA pool operates within a cap over which no borrowing is allowed. This is prescribed by the Government and is set at £66.853m.

2.15 The Cap is shown in the following table with a comparison to the CFR and expected level of actual debt on the HRA.

HRA Limit on Indebtedness	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
HRA Debt Cap	66,853	66,853	66,853	66,853	66,853	66,853
HRA CFR	61,583	61,583	61,583	61,583	61,583	61,583
Difference	5,270	5,270	5,270	5,270	5,270	5,270
HRA Debt	57,423	57,423	57,423	57,423	57,423	57,423
Borrowing Headroom	**9,430**	**9,430**	**9,430**	**9,430**	**9,430**	**9,430**

2.16 It is expected that the CFR and actual debt on the HRA will remain fairly flat over the current MTFP. However, the HRA Business Plan does allow for additional borrowing up to the HRA's debt cap to utilise the borrowing headroom of £9.43m shown in the preceding table.

2.17 The full implications of future New Build programmes beyond the initial 1st phase are still subject to an options appraisal. This is unlikely to occur in 2015/16 and future treasury management considerations associated with New Build will form part of the options appraisal.

2.18 The next planned major debt repayment is a variable rate loan of £10m in 2022. The HRA Business Plan allows for sums to be set aside from its revenue account, commencing in 2017/18 as a provision to repay this and future loans, in accordance with the debt maturity profile.

Revenue Implications

2.19 The Financial implications of the Council's expected debt management transactions have been included in the MTFP and are summarised in the following table.

Interest Payable and Receivable	2014/15 £'000	2015/16 £'000	2016/17 £'000	2017/18 £'000	2018/19 £'000	2019/20 £'000
General Fund						
Interest Payable	4	4	4	4	4	4
Interest Received	-49	-39	-58	-83	-86	-86
HRA						
Interest Payable	1,874	1,685	2,020	2,120	2,222	2,269
Interest Received	-13	-16	-14	-26	-36	-65

3.0 Current Economic Outlook

3.1 Since early 2013, the UK economy has been steadily growing. However, the latest growth forecasts have recently been revised down from 3% year on year, to 2.7%. It is considered that is due to a slowdown in household consumption, together with a more pessimistic outlook for continuing high employment levels and wage growth.

3.2 In addition, inflationary pressure is currently low with the latest CPI and RPI rates being 0.5% and 1.6% respectively (as at December 2014). These are the lowest rates since May 2000 and are being influenced by the continuing reduction in the price of crude oil feeding into fuel and energy prices.

3.3 Due to the low level of inflation and the factors underpinning the figures, it is considered that interest rates will remain at historically low levels until later in 2015, or even beyond. The current outlook for inflation of 2.5% by 2017/18 means that any interest rate rises will be small (0.25%) and incremental.

3.4 In deciding whether to increase the main Bank Base Rate, the Bank of England's Monetary Policy Committee pays particular attention to the rate of growth and wage inflation. If these were to accelerate sharply over the next year, this could mean a different strategy evolves in order to keep inflation to the Government's average target of 2%.

Borrowing Strategy 2015/16 and Longer-Term Plan

4.1 The only debt outstanding relates to the HRA following the debt take-on as part of the self-financing framework for Council Housing introduced in April 2012. For several years, the Council has not entered into any other long-term borrowing arrangements and has managed new prudential borrowing internally through its cash reserves and balances.

4.2 This has proved to be a cheaper form of borrowing with interest rates historically low, limiting the interest earned by having those reserves on deposit.

Existing Debt

4.3 The General Fund has no significant external borrowing outstanding.

HRA Debt

4.4 Total debt outstanding is £57.423m. Of this debt, £10m is at a variable rate and is forecast to increase from 0.6% in 2014/15, to 1.1% by the end of 2015/16. The remaining balance of the debt is all at fixed rates.

4.5 This debt is due to mature periodically between 2022 and 2042. The HRA Business Plan allows for these repayments by setting-aside resources from 2017/18.

4.6 The HRA debt will be reviewed regularly with the Council's treasury advisors to ensure that the portfolio continues to suit the Council.

4.7 During 2014/15, the Council repaid the only other major debt liability outstanding, i.e. a money market loan of £1m. This was to take advantage of early termination terms offered by the Lender and to save approximately £50,000 per year in future interest charges to 2032.

Debt restructuring

4.8 This will be kept under review and the Council has retained the services of treasury advisors to assist the Council. It is possible that the Council will be in a position to repay debt earlier and may also wish to reschedule some longer-term debt depending on future interest rates.

4.9 Although this is not anticipated over the current MTFP it will be kept under review. Any early repayment or rescheduling decision will be based on a Net Present Value calculation taking into account the relevant premium or discount.

Variable Rate Debt

4.10 As some of the debt is being borrowed at variable rates, this will be kept under closer scrutiny. The cost of this proportion of the portfolio (£10m) is currently contained within the resources of HRA Business Plan. The Plan assumes that the rate on this debt will rise to 2% over the MTFP in accordance with current forecasts for interest rates (it is currently 0.6%).

Additional Borrowing

4.11 The Prudential System for Capital Finance provides flexibility for local authorities to borrow within their overall limit. Effectively, councils can borrow money as long as they are able to demonstrate that the associated interest and principal repayments are affordable and sustainable within their longer-term financial resources.

4.12 Additional borrowing can also be undertaken on an “invest to save” basis, i.e. the cost of loan finance is met from the payback of the investment (efficiencies or additional income, etc.).

4.13 The Council has already approved (October 2014) some prudential borrowing, internally, to help deliver a major capital project in 2015/16. The effects of this borrowing have been included in the treasury indicators and the MTFP.

4.14 The HRA self-financing framework provides an opportunity for the Council to undertake additional borrowing as detailed in Section 2 (above). Although this is not anticipated over the current MTFP, it will be kept under review in accordance with the HRA’s Business Plan requirements.

Borrowing in Advance

4.15 The Council will only borrow in advance of need if it is felt that the benefits of borrowing at interest rates now, compared to where they are expected to be in the future, outweighs the current cost and risks associated with investing the proceeds until the borrowing was actually required. Any accounting matters and the general legality will also be considered on a case by case basis.

4.16 In summary, the key matters in the borrowing strategy for 2015/16 are as follows:

- Meeting the Council’s cash flow requirements (*although this will be primarily through its Investment Strategy in Sections 6 and 7*).

- Keeping under review the HRA debt pool and in particular the variable rate borrowing.

5.0 Treasury Management Prudential Indicators and Limits on Activity

5.1 The purpose of these additional indicators is to contain the activity of the treasury function within certain limits, thereby managing risk and reducing the impact of an adverse movement in interest rates.

5.2 However, if these are set too restrictively, they could impede the opportunity to reduce debt costs. The indicators are detailed in the following sections.

Upper limits on variable interest rate exposure

5.3 This indicator identifies a maximum limit for variable interest rates based upon the debt position net of investments. This is set at **5%** and is based on the affordability in the HRA Business Plan. This remains unchanged from that previously.

Upper limits on fixed interest rate exposure

5.4 This is set at **4.5%** and again is based on the affordability of the HRA Business Plan. This also remains unchanged from that previously.

Maturity structure of Fixed Rate Borrowing

5.5 Based on the HRA debt take-on and the money market loan outstanding, the maturing structure is as follows:

Under 12 months	0%
12 months to 2 years	0%
2 years to 5 years	0%
5 years to 10 years	35%
10 years and above	65%

5.6 Although all fixed rate debt is expected to be repaid beyond 10 years, this is spread over a period up to a maximum of 28 years.

Total principal funds invested for greater than 364 days.

5.7 This indicator does not apply to the Council.

6.0 Investment Counterparty and Liquidity Framework

6.1 In accordance with Government Guidance, the primary principle governing the Council's investment criteria is the security and liquidity of its investments. Once that principle is achieved, then yield and length of investment are considered. The Council will also ensure that:

- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the Specified and Non-Specified investment sections below.

Specified Investments

6.2 The purpose of specified investments is to identify investments offering high security and high liquidity. These investments should be in pounds sterling and with a maturity of no more than a year. They are intended to be used with minimal procedural formalities. Any investments made with the UK Government, another local authority or parish council automatically counts as specified investments.

6.3 In addition, short-term investments with bodies with "high credit ratings" will count as specified investments. It is left to each authority to determine these institutions, and the Council must determine investment limits, maximum periods and monitoring arrangements.

Non-Specified Investments

6.4 These are all other investments not meeting the criteria of specified investments. Due to the fact that these investments could carry more risk than specified ones, the Council needs to set limits on these investments and determine guidelines on when they should be used.

6.5 The regulations make it clear that they do not wish to discourage authorities from using non-specified investments. The aim is to ensure that proper procedures are in place for undertaking risk assessments of investments made for longer periods or with bodies that do not carry such a high credit rating.

Credit Quality

6.6 The credit worthiness of counterparties remains paramount in any investment decision and this is reflected in the approved lending policy and counterparty list. This is currently pertinent given the restructuring of the banking sector in the UK and the move towards the principle of "bail ins."

6.7 During 2014/15, the Council approved a fundamental shift in its lending policy. This moved away from a traditional model based primarily on credit ratings, to that based on an assessment of a financial institutions' ability to incur losses before a depositor bail-in.

6.8 Besides this, the Council refers to the financial press, any government support for banks and other market data. This is backed up by information and advice from the Council's retained treasury advisors.

6.9 Based on these core principles, the strategy in Section 7 (below) has been adopted.

7.0 Investment Strategy 2015/16

7.1 The Council is expected to have a regular short-term investment requirement to enable it to manage its day-to-day financial affairs. There is no current proposal to enter into longer term and externally managed funds. Where the Council should need to borrow in advance of need, this investment strategy also applies.

7.2 The approved investment policy is based on a counterparty list that has been carefully considered to select those institutions with the best financial structure and the ability to incur losses before a depositor bail-in. This is based on economic data, together with analysis and advice from the Council's treasury advisors.

7.3 The list is kept under review and updated on a quarterly basis depending on the changing circumstances of selected counterparties.

7.4 The approved lending list and policy is shown at **Appendix 3.** In accordance with regulations, it sets out where the Council will invest surplus funds and places limits upon the various institutions.

7.5 A summary of the counterparties is shown in the following table.

Specified Investments	Non Specified Investments
• UK Debt Management Office (DMO) • Local, Police, Fire and Parish Authorities • Lloyds Bank • Bank of Scotland • HSBC • Nationwide Building Society • Standard Chartered • Santander UK	• Goldman Sachs International • Close Brothers • Leeds Building Society • Barclays Bank • Foreign Counterparties (*AAA rated institutions subject to separate approval by the Section 151 Officer*) • Independent Building Societies *(subject to separate approval by the Section 151 Officer)*

General Policy

7.6 As approved, priority is given to specified investments in any investment decision. The length of investment is made in accordance with overall cash flow requirements.

7.7 The policy focuses on the credit quality of investment counterparties rather than amounts invested and returns.

7.8 Where regular investments are made with named financial institutions, this is generally undertaken via instant access accounts. This allows funds to be withdrawn at short notice if the financial situation of these institutions was to change,

Use of Non-Specified Investments

7.9 These are only used as a "lender of last resort." In particular, this may be the case where limits on specified investments are likely to be exceeded and where there is a temporary need to place money.

7.10 It should be noted that the named counterparties are still considered to be fairly low risk for short-term deposits in accordance with the maximum limits and periods set out in Appendix 3.

Use of Treasury Advisors

7.11 The Council uses a firm of advisors on a retained basis. Their role is to provide market analysis and advice, together with literature and updates on key treasury management developments. They do not offer any of their own or 3rd party products/instruments for borrowing or investing.

7.12 They also provide training workshops and seminars. They are appointed through the Council's procurement framework.

Performance Indicators

7.13 The main indicator is for the return on short-term investments to average, over the year, the Market 7-Day Rate, this being a standard measure of performance. Performance in recent years is shown in the following table.

	2007/08	**2008/09**	**2009/10**	**2010/11**	**2011/12**	**2012/13**	**2013/14**
7-Day Rate (target)	5.61%	3.57%	0.39%	0.51%	0.62%	0.51%	0.47%
Actual Rate	5.81%	4.38%	0.72%	0.78%	0.32%	0.31%	0.33%

APPENDIX 3

APPROVED LENDING LIST & POLICY

1. Approved Types of Investment

The Council uses the following types of investment when managing funds:

- Fixed Term Deposits
- On Call Deposits

2. Lending Policy and Counterparty List (last updated October 2014)

Institution	Limit	Maximum Term
Specified Investments		
• UK Debt Management Office (DMO)	**£15m**	364 Days
• Local, Police, Fire and Parish Authorities	**£5m** with anyone Authority	364 Days
Named Counterparties		
• Lloyds Bank • Bank of Scotland • HSBC • Nationwide Building Society • Standard Chartered • Santander UK	**£2m** with anyone Bank	6 months
Non Specified Investments		
Named Counterparties		
• Goldman Sachs International • Close Brothers • Leeds Building Society • Barclays Bank	**£2m** with anyone Bank	100 days
Foreign Counterparties		
• AAA rated institutions (*subject to separate approval by the Section 151 Officer*)	**£1m** with anyone Bank	1 month
Independent Building Societies		
• *subject to separate approval by the Section 151 Officer*	**£1m** with anyone society	1 month