REPORT 4

HARBOROUGH DISTRICT COUNCIL

REPORT TO THE CABINET MEETING OF 7 FEBRUARY 2022

PUBLIC REPORT: Yes

EXEMPT REPORT: No

Report Title	**Treasury Management Strategy and Prudential Indicators 2022/23, and associated documents**
Report Author	Clive Mason, Director, Finance and Assets (S151 Officer)
Purpose of Report	This report details the Council's proposed prudential indicators for the period 2022/23 to 2024/25 and sets out the forecast treasury activities over the same period. It also fulfils four key requirements of local government legislation as follows: • The reporting of the prudential indicators as required by the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities. • The Council's Minimum Revenue Provision (MRP) Policy, which sets out how the Council will pay for capital assets through revenue each year. • The Treasury Management Strategy, in accordance with the CIPFA Code of Practice on Treasury Management in the public services, and • The Annual Investment Strategy in accordance with the Department of Levelling Up, Housing, and Communities (DLUHC, formerly Ministry of Housing, Communities and Local Government (MHCLG)) investment guidance. In addition, this report includes the Councils proposed strategy in respect of the Flexible Use of Capital Receipts.
Reason for Decision	• The Local Government Act 2003, as amended, and supporting regulations requires the Council to "have regard to" the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three

	years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. • The Council is also required by the Local Government Act 2003 to undertake an annual review of its policy for calculating the minimum revenue provision (MRP) for repayment of external debt. • The Act requires the Council to set out its treasury strategy for borrowing and to prepare an Annual Investment Strategy. This sets out the Council's policies for managing its investments and for giving priority to the security and liquidity of those investments.
Portfolio (holder)	Councillor James Hallam, Finance
Corporate Priorities	YOUR COUNCIL: creative, proactive and efficient CO 8 — Deliver Financial Sustainability for the future
Financial Implications	• These are covered in detail in this report. The current investments at 31 December 2021 are attached at **Appendix 7**.
Risk Management Implications	• Management of the Council's financial resources is key to achieving targets set out in the budget. Security of the Council's money in the current banking market is paramount.
Environmental Implications	• None
Legal Implications	• This report covers the requirement for capital financing and treasury management as set out in the Local Government Act 2003 and subsequent Regulations.
Equality Implications	• None
Data Protection Implications	• None
Consultation	• The Prudential Indicators contained within this report have been compiled to take account of the borrowing requirements and available resources determined as part of the Council's capital programme and overall budget setting process. Members and officers have been involved in the budget process from the outset.
Options	• None
Background Papers	• Treasury Management, Prudential Code, and Budget working papers held in Finance.

Appendices	1 Treasury Management Strategy and Prudential Indicators for 2022/23 2 Detailed Criteria for Investment of Surplus Funds 3 Interest Rate Forecasts 4 Economic Background 5 External Debt Analysis 6 Counterparty List 7 Investments at 31 December 2021 8 Prudential Code Definitions 9 Flexible use of Capital Receipts Strategy
Recommendation	• **To approve the capital prudential indicators and limits for 2022/23 to 2024/25 contained within Appendix 1.** • **To approve the Minimum Revenue Provision (MRP) Statement, contained within Appendix 1.** • **To approve the Treasury Management Strategy 2022/23 and the treasury prudential indicators contained in Appendix 1, including the Authorised Borrowing Limit for the Council.** • **To approve the 2022/23 Annual Investment Strategy for treasury investments contained in Appendix 1 and the detailed criteria included in Appendix 2.** • **To approve the inclusion of Market Harborough Building Society on the list of approved counterparties**. • **To approve the Flexible Use of Capital Receipts Strategy.**

Key Facts

Background

1.1 The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low-risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return.

1.2 The second main function of the treasury management service is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council essentially the longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans or using underlying cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

1.3 The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

1.4 CIPFA defines treasury management as:

"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks."

1.5 Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury or non-financial activities, (arising usually from capital expenditure), and are separate from the day-to-day treasury management activities.

1.6 Members in the past have shown their desire to support local business and therefore to include Market Harborough Building Society on the list of Counterparties for the Council in support of the Corporate Priority "a safe, enterprising and vibrant place". As a small Building Society, it does not meet the minimum requirements of the proposed Annual Investment Strategy and as such would normally be excluded. This report asks Members to consider whether they wish to keep Market Harborough Building Society on the counterparty list (showing which counterparties the Council can make investments with) for the financial year 2022/23 subject to a monetary limit of £2 million.

Reporting Requirements

1.7 **Capital Strategy**: The CIPFA 2017 Prudential and Treasury Management Codes require all local authorities to prepare a capital strategy report, which will provide the following:

(a) a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services

(b) an overview of how the associated risk is managed
(c) the implications for future financial sustainability

1.8 The aim of this capital strategy is to ensure that all elected members on the full council fully understand the overall long-term policy objectives and resulting capital strategy requirements, governance procedures and risk appetite.

1.9 **Treasury Management Reporting**:
The Council is required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals.

1.10 **Prudential and treasury indicators and treasury strategy** (Appendix 1) - The first, and most important report is forward looking and covers:

- the capital plans, (including prudential indicators).
- a minimum revenue provision (MRP) policy, (how residual capital expenditure is charged to revenue over time).
- the treasury management strategy, (how the investments and borrowings are to be organised), including treasury indicators, and
- an investment strategy, (the parameters on how investments are to be managed

1.11 **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

1.12 **An annual treasury report** – This is a backward-looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

1.13 **Scrutiny**: The above reports are required to be adequately scrutinised before being recommended to the Council.

Significant Changes

1.14 **Multi-asset vehicles** have been added to the types of investment listed in the Criteria for Investment detailed in **Appendix 2**. This is because the Director of Finance and Assets has commissioned a review of the Council's investments by its treasury advisors, Link Group, with a view to diversifying by investing in multi-asset vehicles to gain improved returns. Multi-asset vehicles are a combination of asset classes (such as cash, equity or bonds) and provide a greater degree of diversification than investing in a single asset class. Review of the long- term cash flow has revealed up to £6 million is available to invest in a risk managed way.

1.15 **MRP policy,** a change to this was approved by Council in December 2021. The method used to calculate MRP has been revised, and the change has been embedded in the 2022/23 policy detailed in **Appendix 1.**

<u>2021 revised CIPFA Treasury Management Code and Prudential Code</u>

1.16 CIPFA published the revised codes on 20th December 2021 and has stated that formal adoption is not required until the 2023/24 financial year. This Council has to have regard to these codes of practice when it prepares the Treasury Management Strategy Statement and Annual Investment Strategy, and also related reports during the financial year, which are taken to Full Council for approval.

1.17 The revised codes will have the following implications:

- a requirement for the Council to adopt a new debt liability benchmark treasury indicator to support the financing risk management of the capital financing requirement.
- clarify what CIPFA expects a local authority to borrow for and what they do not view as appropriate. This will include the requirement to set a proportionate approach to commercial and service capital investment.
- address environmental, social and governance (ESG) issues within the Capital Strategy.
- require implementation of a policy to review commercial property, with a view to divest where appropriate.
- create new Investment Practices to manage risks associated with non-treasury investment (similar to the current Treasury Management Practices (TMPs)).
- ensure that any long-term treasury investment is supported by a business model.
- a requirement to effectively manage liquidity and longer-term cash flow requirements.
- amendment to TMP1 to address ESG policy within the treasury management risk framework.
- amendment to the knowledge and skills register for individuals involved in the treasury management function - to be proportionate to the size and complexity of the treasury management conducted by each council.
- a new requirement to clarify reporting requirements for service and commercial investment, (especially where supported by borrowing/leverage).

1.18 In addition, all investments and investment income must be attributed to one of the following three purposes: -

Treasury management
Arising from the organisation’s cash flows or treasury risk management activity, this type of investment represents balances which are only held until the cash is required for use. Treasury investments may also arise from other treasury risk management activity which seeks to prudently manage the risks, costs or income relating to existing or forecast debt or treasury investments.

Service delivery
Investments held primarily and directly for the delivery of public services including housing, regeneration and local infrastructure. Returns on this category of investment which are funded by borrowing are permitted only in

cases where the income is “either related to the financial viability of the project in question or otherwise incidental to the primary purpose”.

Commercial return
Investments held primarily for financial return with no treasury management or direct service provision purpose. Risks on such investments should be proportionate to a council’s financial capacity – i.e., that ‘plausible losses’ could be absorbed in budgets or reserves without unmanageable detriment to local services. An authority must not borrow to invest primarily for financial return.

1.19 As this Treasury Management Strategy Statement and Annual Investment Strategy deals solely with treasury management investments, the categories of service delivery and commercial investments will be dealt with as part of the Capital Strategy report. However, as investments in commercial property have implications for cash balances managed by the treasury team, it will be for each authority to determine whether they feel it is relevant to add a high-level summary of the impact that commercial investments have, or may have, if it is planned to liquidate such investments within the three-year time horizon of this report, (or a longer time horizon if that is felt appropriate).

Members will be updated on how all these changes will impact our current approach and any changes required will be formally adopted within the 2023/24 TMSS report.

Flexible Use of Capital Receipts

1.20 The Council approved its Flexible Use of Capital Receipts Strategy in June 2021. This is the last year of the current approved freedom. However, indications from government directly to the Council are that the freedom will be renewed but local government is awaiting the formal guidance. This freedom will allow the Council to finance its Transformation programme, and this is shown in the Draft 2022/23 Capital Programme. In case the freedom is not renewed, then the Council is also maintaining a Transformation Earmarked Reserve. The Strategy itself is shown at **Appendix 9**.