MAIDSTONE BOROUGH COUNCIL

COUNCIL

2 MARCH 2016

REPORT OF THE AUDIT, GOVERNANCE AND STANDARDS COMMITTEE HELD ON 18 JANUARY 2016

TREASURY MANAGEMENT STRATEGY 2016/17

Issue for Decision

In accordance with CIPFA's Code of Practice on Treasury Management, the Council is asked to adopt the Treasury Management Strategy for 2016/17, including the Treasury Management and Prudential Indicators.

Recommendation Made

That the Treasury Management Strategy 2016/17, including the Treasury Management and Prudential Indicators, attached at **Appendices A and B**, be adopted.

Reasons for Recommendation

The Council has adopted CIPFA's Code of Practice on Treasury Management which requires an annual report on the strategy and plan to be pursued within the coming year to be made to full Council.

The Council is required to operate a balanced budget which broadly means that cash raised during the year will meet cash expenditure. The Treasury Management Strategy assists the Council in achieving this objective while maintaining value for money.

The first function of the Council's 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.

The second main function of the Council's Treasury Management operation is the funding of the Council's capital plans. These capital plans provide a guide to the borrowing need of the Council and inform 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 longer term cash flow surpluses.

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".

The Strategy for 2016/17 is set out at **Appendix A** to this report. It is consistent with the requirements of CIPFA and the Department for Communities and Local Government, and it has been developed in line with currently endorsed spending and financing proposals.

In 2012, the Council approved in principle expenditure of up to £6m through prudential borrowing for the acquisition of commercial property, the acquisition of property to alleviate homelessness and action to enable stalled development to progress.

To date, the Council has not borrowed to finance the Capital Programme as the value of borrowing was outweighed by the benefit of using the Council's own resources due to the variance between borrowing and lending rates of interest.

The Policy and Resources Committee, at its meeting held on 27 January 2016, endorsed a Capital Programme for the period 2016/17 to 2020/21. This Programme proposes a significant increase in prudential borrowing to support the regeneration and commercial objectives of the Council, and the prudential borrowing limits set out in the attached Strategy and the Prudential Indicators attached at **Appendix B** have been amended to reflect this.

The maximum prudential borrowing, set at £38,475,000, and other funding proposed in the Capital Programme is as follows:

	2016/17 £	**2017/18 £**	**2018/19 £**	**2019/20 £**	**2020/21 £**
Prudential Borrowing	11,950,000	15,525,000	11,000,000	0	0
Other Funding Streams	8,879,610	4,175,000	2,641,100	2,314,000	1,815,000
Total Programme	20,829,610	19,700,000	13,641,100	2,314,000	1,815,000

In considering the Treasury Management Strategy for 2016/17, the Audit, Governance and Standards Committee was made aware of the potential for this increased level of prudential borrowing. The Committee expressed concern about the risks associated with prudential borrowing of this magnitude. These include:

a) The potential interest rates for long term borrowing in the future;

b) The initial cost of borrowing during the period leading up to the receipt of a return on the scheme as this would not be financed by the scheme at the time that it required payment; and

c) The scheduling of the demand for prudential borrowing over the period of the Capital Programme as the indicative figures show a significant increase in the early years of the Programme.

Whilst these are significant risks, the Audit, Governance and Standards Committee, in endorsing the Treasury Management Strategy, was mindful that mitigation would be considered on a scheme by scheme basis and individual business cases should address these risks in line with the principles set out in the Medium Term Financial Strategy for capital.

The Committee also requested that the ratio of capital financing costs to the net revenue stream (revenue budget) be quantified, and this has been addressed in the attached Strategy and Indicators.

Alternatives Considered and Why Not Recommended

Option 1: The Audit, Governance and Standards Committee could have decided not to recommend the Treasury Management Strategy to the Council. However, the Council must adopt a Strategy for 2016/17, and the Strategy is in line with the necessary codes and practice guides and takes a low risk approach favouring liquidity over return and as such is considered suitable for this Council.

Option 2: Subject to any legal obligations placed upon the Council, the Audit, Governance and Standards Committee could have amended the Strategy prior to submission to the Council providing detailed reasons for the amendment and the risks and benefits that the proposed amendment provided in order for the Council to make a fully informed decision on the recommendation. Areas where amendments could have been made include the following, which are detailed along with reasons for not changing the Strategy:

Limits - The proposed Strategy allows maximum investments with certain institutions of £8m. The current limit could be retained, increased or reduced. Given the difficulty in identifying opportunities to lend at suitable rates within the counterparty list, it is considered appropriate to incorporate sufficient flexibility by retaining the current limit for investments with the most secure organisations.

Counterparties - The proposed Strategy allows non-specified investments with other local authorities and the top five building societies. The Strategy could propose to utilise additional counterparties from the non-specified investments group. However, due to the fact that this would involve an increased level of risk to the security of the Council's cash, this is not considered to represent a prudent course of action.

Alternative Use of Cash - The resources invested in expenditure could be used to deliver key priority outcomes. However, the core cash held by the Council is either set aside for future expenditure, such as the Capital Programme, or held as a form of risk mitigation, such as the minimum level of revenue balances. To use these resources for alternative projects could compromise liquidity and put the Council at future risk should an unforeseen event occur.

External Fund Managers - By appointing external managers local authorities may possibly benefit from security of investments, diversification of investment instruments, liquidity management and the potential of enhanced returns. Managers do operate within the parameters set by local authorities but this involves varying degrees of risk. This option has been discounted on the basis of the risk which would make it difficult to ascertain a suitable sum to assign to an external manager.

Background Papers

None