A&G 25 06 14
Item 7

TREASURY MANAGEMENT OUTTURN 2013/14

EXECUTIVE MEMBER:	Cllr Gillian Troughton
LEAD OFFICER:	Angela George – Interim FMS
REPORT AUTHOR:	Ann Treble, Accountant Financial Management and Treasury

SUMMARY:

The treasury management outturn report was considered by the Executive at their meeting on 27 May 2014 and this report summarises the Executive's recommendations to Council who met on 19 June 2014. As detailed in our Treasury Management Strategy and as required under The Code, this report has to be considered by the Audit & Governance Committee before being recommended to Full Council. This report is to be scrutinised by Audit & Governance Committee and Council gave approval that the portfolio holder in conjunction with the section 151 Officer be delegated authority to fully approve the out-turn subject to the outcome of scrutiny, as per paragraph 4.1.

RECOMMENDATION:

That Audit & Governance Committee note the recommendations to Council to approve the following:

(i) Approve the actual 2013/14 prudential and treasury indicators in paragraph 4.3

Appendix A
EXE 27 05 14

TREASURY MANAGEMENT OUTTURN 2013/14

EXECUTIVE MEMBER:	Councillor Gillian Troughton
LEAD OFFICER:	Angela George, Financial Services Manager/Darienne Law, Interim Manager
REPORT AUTHOR:	Leanne Barwise – Senior Accounting Officer

Why has this report come to the Executive?

This Council is required by regulations issued under the Local Government Act 2003 to produce an annual treasury management review of activities and the actual prudential and treasury indicators for 2013/14. This report meets the requirements of both the CIPFA Code of Practice on Treasury Management (the Code) and the CIPFA Prudential Code for Capital Finance in Local Authorities (the Prudential Code). As detailed in our Treasury Management Strategy and as required under The Code, this report has to be considered by the Audit & Governance Committee before being recommended to Council. It will therefore be considered for scrutiny on 25th June 2013. It is recommended that the Portfolio holder, in conjunction with the Section 151 Officer, be delegated authority to fully approve the outturn subject to the outcome of the scrutiny of Audit & Governance Committee.

Recommendations:

The Executive are asked to make a recommendation to Council to:

(i) Approve the actual 2013/14 prudential and treasury indicators attached at Appendix A.
(ii) Note the Treasury Management Outturn 2013/14 detailed in Section 9 of this report.
(iii) Note the make-up of the portfolio of investments as at 31st March 2014 attached at Appendix B.
(iv) Note and approve the clarification to the Treasury Management Strategy Statement 2014/15 as approved in February 2014 detailed in paragraph 10.
(v) Note that this report will be formally considered by the Audit & Governance Committee on 25th June and delegate authority to the Portfolio holder in conjunction with the Section 151 Officer to approve the outturn after scrutiny.

1. Introduction

Copeland Borough Council received £31m in April 2013 and 2014, being a full year payment of National Non Domestic Rates (NNDR) from one ratepayer. Whilst this is received by the Authority, it does not all actually belong to the authority. We collect NNDR on behalf of Central Government and Cumbria County Council (CCC) and are only entitled to retain our "baseline need" amount (subject to safety net). The authority also receives further NNDR throughout the year of approximately £4.5m, but similarly this is not all the Authority's funding. The Authority is required to distribute the NNDR it receives to Government and to CCC on a monthly basis. The yearly amount is circa £28m but this is paid out in (varying) monthly payments to DCLG & CCC. These payments may result in monies owed to DCLG and CCC if NNDR collected exceeds the amount anticipated or alternatively would result in additional funds being owed to this authority in respect of (enhanced) safety net payments if collection is below the anticipated amount.

We receive Council Tax receipts monthly with council tax payers having the option to pay over 10 or 12 months. This also is not the Councils funds to keep and some must be repaid to our main preceptors, Cumbria County Council and the Police and Crime Commissioner at £1.9m and £0.3m per month respectively (£26.4m per year). The Council retains only its share, circa £3.5m.

Copeland Borough Council holds an average investment portfolio of £20-25m of its own funds (reducing as used). This funding is essential to running the organisation and is placed as investments only until it is required. The funds back up the authority's balance sheet and comprise (roughly) of:

Description of funds held	£'000ms*
General fund reserve (used to balance revenue budget and mitigate risks identified)	3.8
Earmarked reserve (held for specific activities/projects)	5.7
Useable Capital Receipts Reserve (for capital expenditure only)	3.6
Loan Principle (to be repaid when loan redeemed)	5.0
Working Capital (to provide cashflow to Council to pay invoices before funds received)	1.9**
Core funds held – invested until required	20.0

*Balances are approximate at 31/03/14 and will fluctuate throughout the year and from year to year dependent upon usegae and receipt.
**estimate

As detailed in the paragraph earlier, we receive a full year payment of NNDR which results in a total portfolio in the region of £54m.

The balances held as at 31 March 2014 are higher than the previous year. This is due to the receipt of National Non-Domestic Rates (NNDR) that has not been paid over to the preceptors as it is anticipated it will be required to repay a rate payer who has lodged an appeal. If this appeal is successful this money will be paid to the rate payer (value may be higher) and so it is not Copeland's money. Should the appeal be unsuccessful, or successful but at a lower value, any money not repaid to the rate payer will be due to Cumbria County Council (10% as preceptor) and Central Government (50% as major preceptor and remaining as levy and/or as repayment of safety net payments made to Copeland).

The regulatory environment places responsibility on Members for the review and scrutiny of treasury management policy and activities. This report is important in that respect, as it provides details of the outturn position for treasury activities and highlights compliance with the Council's policies previously approved by Members.

During 2013/14 the minimum reporting requirements were that Council should receive the following reports:

- an annual treasury strategy in advance of the year (Council 21st February 2013)
- a mid-year (minimum) treasury update report (Council 5th December 2013)
- an annual review following the end of the year describing the activity compared to the strategy (this report)

In addition, this Council has received quarterly treasury management update reports on 27th August 2013 and 17th February 2014 which were presented to Executive.

This Council also confirms that it has complied with the requirement under the Code to give prior scrutiny to the reports by the Audit & Governance Committee before being reported to Council (wherever possible). This report will be presented to Audit Committee on 25th June 2014.

Member training on treasury management issues was undertaken prior to Audit Committee on 30th January 2014 in order to support Members' scrutiny role. Another annual training session will be arranged for the 2014/15 financial year as part of the ongoing Treasury Management training program for Members and Officers.

2. The Economy and Interest Rates

The financial year 2013/14 continued the challenging investment environment of previous years. Investment returns remained low although levels of counterparty risk had subsided these still remained at uncomfortable levels. The original expectation for 2013/14 was that Bank Rate would not rise during the year and for it only to start gently rising from quarter 1 2015. This forecast rise has now been pushed back to a start in quarter 3 2015. Economic growth (GDP) in the UK was virtually flat during 2012/13 but recovery took hold in 2013/14, returning to more normal levels, albeit from a very low base. As a consequence there was no additional quantitative easing during 2013/14 and Bank Rate ended the year unchanged at 0.5% for the fifth successive year. While CPI inflation had remained above the 2% target during 2012, by January 2014 it had fallen to 1.9% and then fell further to 1.7% in February. It is expected to remain slightly below the target rate for most of the two years ahead.

UK Government bond yields (Gilt yields), underpin the Authority's borrowing, and were on a sharply rising trend during 2013 until market concerns returned in the first quarter of 2014 in emerging markets and the Crimea, sparking a flight to quality (see paragraph 4.). This is where investors shun certain investment areas and put funds into perceived less risky areas, such as the UK.

The Funding for Lending Scheme, announced in July 2012, resulted in a flood of cheap credit being made available to banks which then resulted in money market investment rates falling drastically in the second half of that year and continuing into 2013/14. The part of the Scheme which supported the provision of credit for mortgages was terminated in the first quarter of 2014 as concerns rose over resurging house prices.

The UK coalition Government maintained its tight fiscal policy stance but recent strong economic growth has led to a cumulative, , reduction in the forecasts for total borrowing, of £97bn over the next five years, culminating in a £5bn surplus in 2018-19, as set out in the Autumn Statement and the March Budget.

The EU sovereign debt crisis subsided during the year and confidence in the ability of the Eurozone to remain intact increased substantially. Perceptions of counterparty risk improved after the European Central Bank (ECB) statement in July 2012 that it would do "whatever it takes" to support struggling Eurozone countries; this led to a return of confidence in its banking system which has continued into 2013/14 and led to a move away from only very short term investing. However, the problems of the Eurozone, or its banks, have not ended as growth is expected to be weak over the next few years as the total size of government debt for some nations is likely to continue rising.

3. Overall Treasury Position as at 31st March 2014

At the beginning and the end of 2013/14 the Council's treasury position (excluding borrowing by PFI and finance leases) was as follows:

		31st March 2013 Principal	Rate/ Return	Average Life (Years)	31st March 2014 Principal*	Rate/ Return	Average Life (Years)
Total debt (Fixed rate funding)	*A*	*£5.00m*	*7.55%*	*29*	*£5.00m*	*7.55%*	*28*
CFR	*B*	*£8.47m*			*£7.93m*		
Less PFI Liability	*C*	*(£6.11m)*			*(£5.81m)*		
Less Vehicle Leases	*D*	*(£0.82m)*			*(£0.57m)*		
Residual need to borrow	*E = b-c-d*	*£1.54m*			*£1.55m*		
Over / (under) borrowing	*F = a-e*	*£3.47m*			*£3.45m*		
Total investments	*G*	*£18.45m*			*£25.67m*		
Net debt	*H = a+c+d-g*	*(£6.51m)*			*(£14.29m)*		

*subject to Audit

4. The Strategy for 2013/14

The expectation for interest rates in the strategy for 2013/14 was a low but rising Bank Rate (starting in quarter 1 of 2015) with similar gradual rises in medium and longer term fixed borrowing rates during 2013/14. Variable or short-term rates were expected to be the cheaper form of borrowing (if necessary) over the period. Continued uncertainty in the aftermath of the 2008 financial crisis promoted a cautious approach, whereby investments would continue to be dominated by low counterparty risk considerations, resulting in relatively low returns compared to borrowing rates.

The strategy remained relatively unchanged, reflecting the heightened uncertainty in the current economic market. The tightened restrictions on our investment criteria remained and we utilised "safe havens", being UK semi-nationalised institutions (RBS & Lloyds/BOS Group), additional Money Market Funds (highly rated liquid institutions) or instant access accounts with Banks. This ensured there was a balance between security and liquidity of funds and the yield achieved, with security being the principle concern particularly in the current economic climate.

5. The Borrowing Requirement and Debt

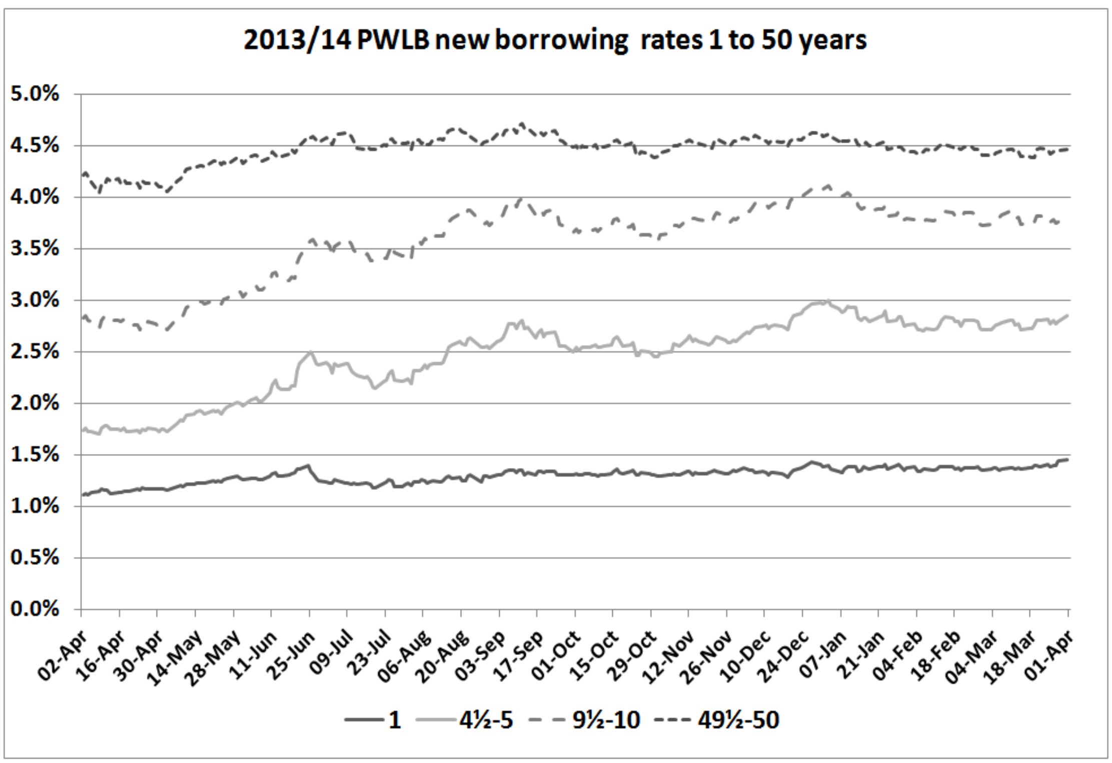
The Council's underlying need to borrow to finance capital expenditure is termed the Capital Financing Requirement (CFR).

	31 March 2013 Actual	31 March 2014 Estimate	31 March 2014 Actual
Total CFR	£8.47m	£7.91m	£7.93m*

*subject to audit

6. Borrowing Rates in 2013/14

PWLB borrowing rates - the graph below shows how PWLB certainty rates have risen from historically very low levels during the year.



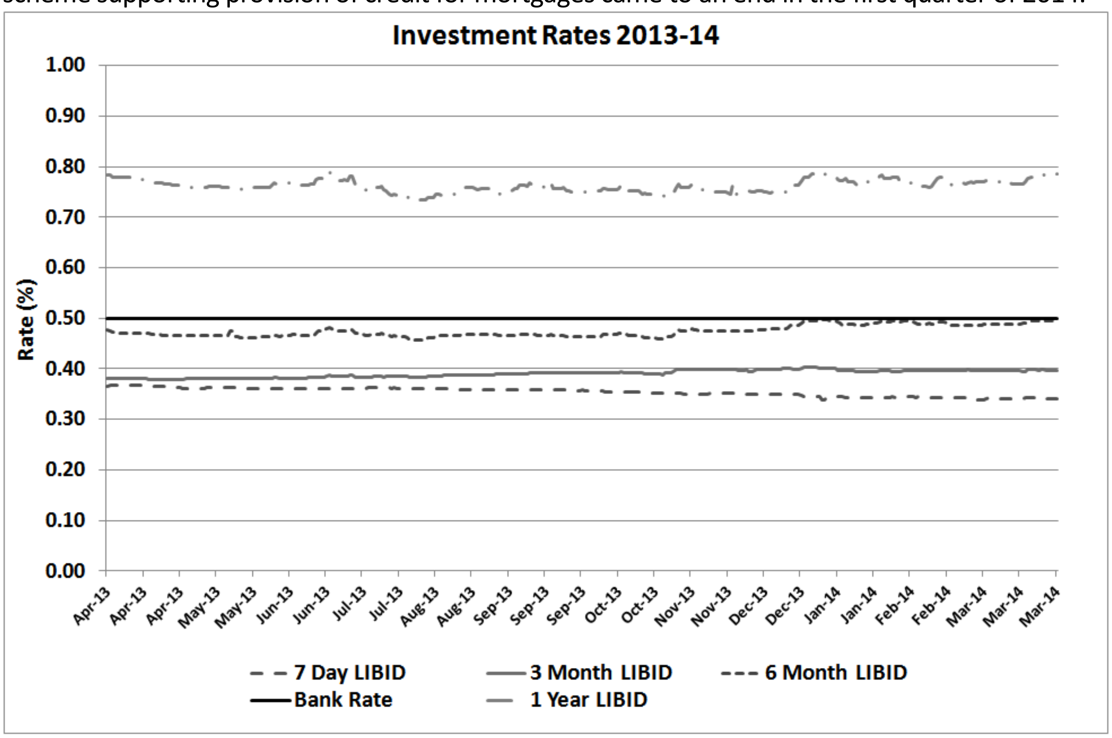
7. Borrowing Outturn for 2013/14

Borrowing – The Council only has one remaining market loan in its debt portfolio as detailed below. We continually assess the position of this loan with our Treasury Consultants, Capita, to ensure we are securing the best terms for the Council. At the current time, the advice is to leave the loan in its present form, as the penalty for repaying early would be prohibitive. It is anticipated as interest rates rise it will become economically beneficial to repay the loan but the timing of this is not predictable.

Lender	Principal	Date Advanced	Type	Interest Rate	Years to Maturity	Date of Maturity
Market	£5.00m	01/02/2002	Fixed interest rate	7.55%	28 years	01/02/2042

8. Investment Rates in 2013/14

Bank Rate remained at its historic low of 0.5% throughout the year; it has now remained unchanged for five years. Market expectations are that this will remain unchanged until early 2015. The Funding for Lending Scheme depressed deposit rates during the whole of the year, although the part of the scheme supporting provision of credit for mortgages came to an end in the first quarter of 2014.



9. Investment Outturn for 2013/14

Investment Policy – the Council's investment policy is governed by CLG guidance, which was implemented in the annual investment strategy approved by the Council on 21st February 2013. This policy set out the approach for choosing investment counterparties, and based on credit ratings provided by the three main credit rating agencies supplemented by additional market data (such as rating outlooks, credit default swaps, bank share prices etc). Operationally, however, within the strategy we temporarily restricted the use of Building Societies (removed from 2014/15 Strategy) and other lower rated institutions and ensured funds were only placed with semi-nationalised institutions, higher rated banks or Money Market Funds and instant access accounts.

The Council had no liquidity difficulties and the investment activity during the year conformed to the approved strategy with the exception of the following:-

- An error with one of our Money Market Funds processing two transactions incorrectly resulted in the return of our investment to our Natwest Account. As the receipt was only discovered/received after the trading deadline of 1pm the balance had to remain in our Natwest Account overnight. The funds were transferred to our Special Interest Bearing Account at a rate of 0.25% until the Money Market Fund opened for trading the following day. This was an overnight breach of our self-imposed counterparty limit as NatWest is part of the Royal Bank of Scotland (RBS) and we would normally reduce the balance within our NatWest Account to a minimum level to remain within these limits.

Investments held by the Council - Over the full financial year, the Council maintained an average balance of £40m of internally managed funds (not all of which are Copeland's, please see paragraph 1). The actual interest earned for 2013/14 was £212,783 (as reported in the Revenue Out-turn Report) against a budgeted return of £202,822, resulting in a small net improvement against the budgeted return on investments for 2013/14 of £9,961. The Treasury Management Strategy 2013/14 remained unchanged since its approval in February 2013. The continuing low interest rates which fell further during the year as a result of the Funding for Lending Scheme afforded the small return. This compares to actual interest earned in 2012/13 of £288,585 against a budget estimate of £227,822, resulting in an overachievement of income of £60,763.

The internally managed funds earned an average rate of return of 0.54% over the 2013/14 financial year. Whilst above base rate at 0.50%, it is much lower than historical trends. This is due to the economic climate and the reduction in rates offered by the banks whilst they have access to cheaper borrowing through the Funding for Lending Scheme. In light of the continued reduction in investment income over the years the 2014/15 budget for investment returns has been reduced by £50k to £152,822 with the expectation that the rates that were achieved in previous years (highest rate achieved 2013/14 was 1.05%) will not be available in 2014/15.

10. The Treasury Management Strategy 2014/15

The Treasury Management Strategy Statement 2014/15 (TMSS) was approved at Council 27th February 2014 with some revisions to aid the placing of funds in the current climate. One revision (recommendation (iv) of the TMSS 14/15) was the change in our criteria requiring counterparties we use to have a Financial Strength rating of C- (long term viability rating) as opposed to C to allow investments with two further counterparties (Barclays & Santander). To mitigate any potential risk to the authority by widening these criteria; it was approved that all investments placed with these counterparties would be restricted to 100 days.

The banks to be used are classed as medium quality and the table that appeared in the TMSS 2014/15 is detailed below:

Sector Limits	Fitch Long term Rating (or equivalent)	Money and/or % Limit	Time Limit
Banks 1 higher quality	*AA-*	£5m	3yrs
Banks 1 medium quality	*A-*	£3m	1yr
Banks 2 – part nationalised	-	£10m	1yr
Limit 3 category – Council's banker (not meeting Banks 1)	-	£10k	1 day
Other institutions limit	-	£2m	1yr
DMADF	AAA	unlimited	6 months
Local authorities	N/A	£5m	1yr
Money market funds (SNAV and VNAV)	AAA	£5m	liquid
Enhanced money market funds	AAA	5 / 10%	liquid

However, the correct interpretation of this change in strategy in February 2014 is as detailed below:-

Sector Limits	Fitch Long term Rating (or equivalent)	Money and/or % Limit	Time Limit
Banks 1 higher quality	*AA-*	£5m	3yrs
Banks 1 medium quality	*A-*	£5m	100 days
Banks 2 – part nationalised	-	£10m	1yr
Limit 3 category – Council's banker (not meeting Banks 1)	-	£10k	1 day
Other institutions limit	-	£2m	1yr
DMADF	AAA	unlimited	6 months
Local authorities	N/A	£5m	1yr
Money market funds (SNAV and VNAV)	AAA	£5m	liquid
Enhanced money market funds	AAA	5 / 10%	liquid

This will allow investments with any counterparties that fall within these limits of up to £5m but restricted to no longer than 100 days.

11. Conclusion

The Council has complied with all of the relevant statutory and regulatory requirements which require the Council to identify and, where possible, quantify the levels of risk associated with its treasury management activities. In particular, its adoption and implementation of both the Prudential Code and the Code of Practice for Treasury Management means both that its capital expenditure is prudent, affordable and sustainable, and its treasury practices demonstrate a very low risk approach.

12. Statutory Officer Comments

12.1 The Monitoring Officer's comments are:

12.2 The Section 151 Officer's comments are: Included in this report

12.3 Other consultee comments, if any:

12.4 Policy Framework comments:

13. How will the proposals be project managed and how are the risks going to be managed?

The Council's treasury management activities are regulated by a variety of professional codes and statutes and guidance:

- The Local Government Act 2003 (the Act), which provides the powers to borrow and invest as well as providing controls and limits on this activity;
- The Act permits the Secretary of State to set limits either on the Council or nationally on all local authorities restricting the amount of borrowing which may be undertaken;
- Statutory Instrument (SI) 3146 2003, as amended, develops the controls and powers within the Act;
- The SI requires the Council to undertake any borrowing activity with regard to the CIPFA Prudential Code for Capital Finance in Local Authorities;
- The SI also requires the Council to operate the overall treasury function with regard to the CIPFA Code of Practice for Treasury Management in the Public Services;
- Under the Act the CLG has issued Investment Guidance to structure and regulate the Council's investment activities.

Under section 238(2) of the Local Government and Public Involvement in Health Act 2007 the Secretary of State has taken powers to issue guidance on accounting practices.

List of Appendices

Appendix A – Prudential & Treasury Indicators
Appendix B - Temporary Investments as at 31st March 2014

Appendix A

Capital Prudential and Treasury Indicators

The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential code and produce prudential indicators. Each indicator either summarises the expected capital activity or introduces limits upon that activity, reflecting the outcome of the Council's underlying capital appraisal systems.

During 2013/14, this Council has complied with its legislative and regulatory requirements i.e. the Capital Prudential Indicators that were set at Full Council within the Treasury Management Strategy 2013/14 on 21st February 2013. The key actual prudential and treasury indicators detailing the impact of capital expenditure activities during the year, with comparators, are as follows:

A. **Gross borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term and are only for a capital purpose, the Council should ensure that its gross external borrowing does not, except in the short term, exceed the total of the capital financing requirement in the preceding year (2012/13) plus the estimates of any additional capital financing requirement for the current (2013/14) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. This indicator allows the Council some flexibility to borrow in advance of its immediate capital needs in 2013/14. ***The Council has complied with this indicator as detailed within Table A overleaf.***

B. **The authorised limit** - the authorised limit is the "affordable borrowing limit" required by s3 of the Local Government Act 2003. Once this has been set, the Council does not have the power to borrow above this level. ***Table B demonstrates that during 2013/14 the Council has maintained gross borrowing within our authorised limit.***

C. **The operational boundary** – the operational boundary is the expected borrowing position of the Council during the year. Periods where the actual position is either below or over the boundary is acceptable subject to the authorised limit not being breached. ***See Table B for the 2013/14 out turn position of the operational boundary.***

D. **Actual financing costs as a proportion of net revenue stream** - this indicator identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Table A

Actual prudential and treasury indicators	Ref	2012/13 Actual £m	2013/14 Original Estimate* £m	2013/14 Actual* £m
Capital expenditure		£1.52m	£1.60m	£0.78m
Capital Financing Requirement		£8.47m	£7.91m	£7.93m
Gross borrowing - External debt	(a)	£11.94m	£10.83m	£11.38m
Investments - Under 1 year	(b)	£18.45m	£14.60m	£25.67m
Net Investments	(a-b)	(£6.51m)	(£3.77m)	(£14.29m)

*Prior to approval of Final Accounts

Table B

Prudential Indicator	2013/14
Authorised limit	£17.00m
Maximum gross borrowing position	£11.94m
Operational boundary	£12.00m
Average gross borrowing position	£11.66m
Financing costs as a proportion of net revenue stream	6.55%

Affordability Prudential Indicators

The previous tables cover the overall capital and control of borrowing prudential indicators, but we are also required to assess the affordability of the capital investment plans. These provide an indication of the impact of the capital investment plans on the Council's overall finances.

The indicator detailed in Table C below, identifies the trend in the cost of capital (borrowing and other long term obligation costs net of investment income) against the net revenue stream.

Table C

Ratio of financing costs to net revenue stream	31 March 2013 Actual	2013/14 Estimate	31 March 2014 Actual
Ratio	7.16%	7.73%	6.55%

The next indicator as detailed in Table D (below) identifies the revenue costs associated with proposed changes to the three year capital programme recommended at Full Council on 21st February 2013 compared to the Council's existing approved commitments and current plans.

Table D

Incremental impact of capital investment decisions	**31 March 2013 Actual**	**2013/14 Original Limits**	**31 March 2014 Actual**
Increase in Council Tax (Band D) per annum	0%	0%	0%

The maturity structure of the debt portfolio was as follows:

	31 March 2013 Actual	**2013/14 Original Limits**	**31 March 2014 Actual**
Under 12 months	100%	100%	100%
12 months and within 5 years	100%	100%	100%
5 years and within 10 years	100%	100%	100%
10 years and within 20 years	100%	100%	100%
21 years and within 30 years	100%	100%	100%
31 years and within 40 years	0	0	0
41 years and above	0	0	0

All investments within the Councils portfolio were placed for under one year. The authority held 100% specified investments at the year-end against a maximum limit of 75% non-specified investments.

The exposure to fixed and variable rate investments was as follows:

	31 March 2013 Actual	**31 March 2014 Actual**
Fixed rate (Principal)	£7.40m	£14.90m
Variable rate (Principal)	£11.05m	£10.77m
TOTAL INVESTMENT	**£18.45m**	**£25.67m**

APPENDIX B

TEMPORARY INVESTMENTS AT 31/03/14

	AMOUNT	PERIOD OF LOAN	VALUE DATE	MATURITY DATE	RATE	BASE RATE
RBS CALL	0	CALL			0.60%	
RBS MMF	868,000	CALL			0.34%	
IGNIS MMF	4,950,000	CALL			0.38%	
BLACKROCK MMF	0	CALL			0.30%	
RBS	7,450,000	90 DAYS FIXED	12/03/2014	10/06/2014	0.80%	
INSIGHT MMF	0	CALL			0.35%	
LLOYDS DEPOSIT	7,450,000	364 DAYS	21/05/2013	20/05/2014	1.05%	
FEDERATED INVESTORS MMF	4,950,000	CALL			0.35%	
LGIM MMF	0	CALL			0.31%	
TOTAL	**25,668,000**				0.69%	0.50%

SUMMARY

	BALANCE	LIMIT	AVAILABLE
DMADF	0	Unlimited	Unlimited
BANK OF SCOTLAND/LLOYDS	7,450,000	10,000,000 *	2,550,000
RBS MMF	868,000	5,000,000	4,132,000
RBS	7,450,000	10,000,000 *	2,550,000
IGNIS MMF	4,950,000	5,000,000	50,000
INSIGHT MMF	0	5,000,000	5,000,000
BLACKROCK MMF	0	5,000,000	5,000,000
FEDERATED INVESTORS MMF	4,950,000	5,000,000	50,000
LGIM	0	5,000,000	5,000,000
	25,668,000	**50,000,000**	**24,332,000**

* Investment limit of £7.5m, however ulitmate limit of upto £10m with prior approval of S151 and for short term investments only.
This has been amended to £10m from 01/04/14 in TMSS 2014/15 approved February 2014.