Treasury Management Strategy Statement and Investment Strategy 2017/18 – Mid-year review

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Purpose of the Report

1. This report has been prepared for Council to approve the mid-year Treasury Management Strategy Statement and Investment Strategy for 2017/18. The revised strategy has already been approved by the Audit Committee on 26th October 2017.

Recommendation(s)

2. The Audit Committee recommends that Council approve the revised Treasury Management Strategy Statement and Investment Strategy for 2017/18 (Strategy attached with the amendments highlighted).

Introduction

3. In March 2011 the Authority adopted the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the Council to approve an annual Treasury Management Strategy and report treasury performance mid-year and at the semi-annual and annual reports.

4. The Treasury Management Strategy Statement (TMSS) for 2017/18 was approved at a meeting of the full Council on 23 February 2017. The Council has invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of risk are therefore central to the treasury management strategy.

Background

5. The Chartered Institute of Public Finance and Accountancy's Code of Practice for Treasury Management in Public Services (the "CIPFA TM Code") and the Prudential Code require local authorities to determine the Treasury Management Strategy Statement (TMSS) and Prudential Indicators (PIs) on an annual basis. The TMSS also includes the Annual Investment Strategy (AIS) that is a requirement of the CLG's Investment Guidance.

6. CIPFA has defined Treasury Management as:

   "the management of the organisation's 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."

7. The Council delegates responsibility for the implementation and monitoring of its treasury management policies and practices to Audit Committee and for the execution and administration of treasury management decisions to the S151 Officer who will act in accordance with the organisation's policy statement and Treasury Management Practices (TMPs), and CIPFA's standard of Professional Practice on Treasury Management.

8. The Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Specific risks are identified in the Council's approved Treasury Management Practices. The risks include:

   - Liquidity Risk (Adequate cash resources)
   - Market or Interest Rate Risk (Fluctuations in the value of investments and borrowing).
   - Inflation Risks (Exposure to inflation)
   - Credit and Counterparty Risk (Security of Investments)
   - Refinancing Risks (Impact of debt maturing in future years).
   - Legal & Regulatory Risk (Compliance with statutory and regulatory requirements).

9. The Local Government Act 2003 requires the Council to 'have regard to' the Prudential Code and to set Prudential Indicators for the next three years to ensure that the Council's capital investment plans are affordable, prudent and sustainable. The Act therefore 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.

10. When the strategy for 2017/18 was written it took into account the Council's current treasury position and drew upon the forecasts for interest rates provided by the Council's treasury advisers, leading to the proposed Prudential Indicators included. This has been amended with the most recent forecast provided by the Council's treasury advisers.

11. The Strategy is attached at Appendix 1 and is split into the following main areas:

    - Background
    - Credit Outlook and Interest Rate Forecast
    - Balance Sheet and Treasury Position
    - Borrowing Requirement and Strategy
    - Investment Strategy
    - Policy on use of financial Derivatives
    - Balanced Budget Requirement
    - 2017/18 MRP Statement
    - Monitoring and Reporting on Treasury Management
    - Other Items

Regulatory Updates

12. **MiFID II**: Local authorities are currently treated by regulated financial services firms as professional clients who can "opt down" to be treated as retail clients instead. But from 3rd January 2018, as a result of the second Markets in Financial Instruments Directive (MiFID II), local authorities will be treated as retail clients who can "opt up" to be professional clients, providing that they meet certain criteria. Regulated financial services firms include banks, brokers, advisers, fund managers and custodians, but only where they are selling, arranging, advising or managing designated investments. In order to opt up to professional, the authority must have an investment balance of at least £10 million and the person authorised to make investment decisions on behalf of the authority must have at least one year's relevant professional experience. In addition, the firm must assess that that person has the expertise, experience and knowledge to make investment decisions and understand the risks involved.

13. The main additional protection for retail clients is a duty on the firm to ensure that the investment is "suitable" for the client. However, local authorities are not protected by the

Financial Services Compensation Scheme nor are they eligible to complain to the Financial Ombudsman Service whether they are retail or professional clients. It is also likely that retail clients will face an increased cost and potentially restricted access to certain products including money market funds, pooled funds, treasury bills, bonds, shares and to financial advice. The Authority has declined to opt down to retail client status in the past as the costs were thought to outweigh the benefits.

14. The Authority meets the conditions to opt up to professional status and intends to do so in order to maintain their current MiFID status.

15. **CIPFA Consultation on Prudential and Treasury Management Codes**: In February 2017 CIPFA canvassed views on the relevance, adoption and practical application of the Treasury Management and Prudential Codes and after reviewing responses launched a further consultation on changes to the codes in August with a deadline for responses of 30th September 2017.

16. The proposed changes to the Prudential Code include the requirement to produce a new high-level Capital Strategy report to full council which will cover the basics of the capital programme and treasury management. The prudential indicators for capital expenditure and the authorised borrowing limit would be included in this report but other indicators may be delegated to another committee. There are plans to drop certain prudential indicators, however local indicators are recommended for ring fenced funds (such as the Housing Revenue Account (HRA) for Council's that retain a council housing landlord function) and for group accounts. Other proposed changes include applying the principles of the Code to subsidiaries.

17. Proposed changes to the Treasury Management Code include the potential for non-treasury investments such as commercial investments in properties to be incorporated within the definition of "investments" as well as loans made or shares brought for service purposes. Another proposed change is the inclusion of financial guarantees as instruments requiring risk management and as such addressed within the Treasury Management Strategy. Approval of the technical detail of the Treasury Management Strategy may be delegated to a committee rather than needing approval of full Council. There are also plans to drop or alter some of the current treasury management indicators.

18. CIPFA intends to publish the two revised Codes towards the end of 2017 for implementation in 2018/19, although CIPFA plans to put transitional arrangements in place for reports that are required to be approved before the start of the 2018/19 financial year. The Department of Communities and Local Government (DCLG) and CIPFA wish to have a more rigorous framework in place for the treatment of commercial investments as soon as is practical. It is understood that DCLG will be revising its Investment Guidance (and its MRP guidance) for local authorities in England; however there have been no discussions with the devolved administrations yet.

Financial Implications

19. There are no additional financial implications in reviewing the attached treasury management strategy.

Background Papers

CIPFA Treasury Management Code of Practice
Treasury Management Practices