

# LEGISLATION AND REGULATIONS IMPACTING ON TREASURY MANAGEMENT

The following items numbered 1 - 4 show the sequence of legislation and regulation impacting on the treasury management function. The sequence begins with primary legislation, moves through Government guidance and Chartered Institute of Public Finance and Accountancy (CIPFA) codes of practice and finishes with implementation through the Council's own Treasury Management Practices.

## **1. Local Government Act 2003**

Link below

### **[Local Government Act 2003](#)**

Below is a summary of the provisions in the Act dealing with treasury management.

In addition the Secretary of State is empowered to define the provisions through further regulations and guidance which he has subsequently done through statutory instruments, Department of Communities and Local Government Guidance and CIPFA codes of practice.

#### **Power to borrow**

The Council has the power to borrow for purposes relevant to its functions and for normal treasury management purposes – for example, to refinance existing debt.

#### **Control of borrowing**

The main borrowing control is the duty not to breach the prudential and national limits as described below.

The Council is free to seek loans from any source but is prohibited from borrowing in foreign currencies without the consent of Treasury, since adverse exchange rate movements could leave it owing more than it had borrowed.

All of the Council's revenues serve as security for its borrowing. The mortgaging of property is prohibited.

It is unlawful for the Council to 'securitise', that is, to sell future revenue streams such as housing rents for immediate lump-sums.

#### **Affordable borrowing limit**

The legislation imposes a broad duty for the Council to determine and keep under review the amount it can afford to borrow. The Secretary of State has subsequently defined this duty in more detail through the Prudential Code produced by CIPFA, which lays down the practical rules for deciding whether borrowing is affordable.

It is for the Council (at a meeting of the full Council) to set its own 'prudential' limit in accordance with these rules, subject only to the scrutiny of its external auditor. The Council is then free to borrow up to that limit without Government consent. The Council is free to vary the limit during the year, if there is good reason.

Requirements in other legislation for the Council to balance its revenue budget prevent the long-term financing of revenue expenditure by borrowing.

However the legislation does confer limited capacity to borrow short-term for revenue needs in the interests of cash-flow management and foreseeable requirements for temporary revenue borrowing are allowed for when borrowing limits are set by the Council.

The Council is allowed extra flexibility in the event of unforeseen needs, by being allowed to increase borrowing limits by the amounts of any payments which are due in the year but have not yet been received.

### **Imposition of borrowing limits**

The Government has retained reserve power to impose 'longstop' limits for national economic reasons on all local authorities' borrowing and these would override authorities' self-determined prudential limits. Since this power has not yet been used the potential impact on the Council is not known.

### **Credit arrangements**

Credit arrangements (eg property leasing, PFI and hire purchase) are treated like borrowing and the affordability assessment must take account not only of borrowing but also of credit arrangements. In addition, any national limit imposed under the reserve powers would apply to both borrowing and credit.

### **Power to invest**

The Council has the power to invest, not only for any purpose relevant to its functions but also for the purpose of the prudential management of its financial affairs.

## **2. Ministry for Communities Housing and Local Government Investment Guidance (revised February 2018)**

The Local Government Act 2003 requires a local authority ".....to have regard (a) to such guidance as the Secretary of State may issue....." and the current guidance became operative on 1 April 2018

The Guidance recommends that for each financial year the Council should prepare at least one investment Strategy to be approved before the start of the year. The Strategy must cover:

- **Investment security**

Investments should be managed prudently with security and liquidity being considered ahead of yield

Potential counterparties should be recognised as "specified" and "non-specified" with investment limits being defined to reflect the status of each counterparty

- **Investment risk**

Procedures should be established for monitoring, assessing and mitigating the risk of loss of invested sums and for ensuring that such sums are readily accessible for expenditure whenever needed.

The use of credit ratings and other risk assessment processes should be explained

The use of external advisers should be monitored

The training requirements for treasury management staff should be reviewed and addressed

Specific policies should be stated as regards borrowing money in advance of need

- **Investment Liquidity**

The Strategy should set out procedures for determining the maximum periods for which funds may prudently be committed

The Strategy should be approved by the full Council and made available to the public free of charge. Subject to full Council approval, or approved delegations, the Strategy can be revised during the year.

### **3. Treasury Management in the Public Services: Code of Practice and Cross-Sectoral Guidance Notes revised (CIPFA 2017)**

The primary requirements of the Code are:

- Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.
- Creation and maintenance of Treasury Management Practices ("TMPs") that set out the manner in which the Council will seek to achieve those policies and objectives.
- Receipt by the full Council or Cabinet of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Half-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.
- Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
- Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body.

### **4. The Prudential Code for Capital Finance in Local Authorities (CIPFA 2011) – Guidance revised 2017**

Compliance with the objectives of the Code by the Council should ensure that:

- Capital expenditure plans are affordable in terms of their implications on Council Tax and housing rents
- External borrowing and other long term liabilities are within prudent and sustainable levels
- Treasury management decisions are taken in accordance with good professional practice

As part of the two codes of practice above the Council is required to:

- agree a series of prudential indicators against which performance is measured
- produce Treasury Management Practice Notes for officers which set out how treasury management policies and objectives are to be achieved and activities controlled.

# TREASURY MANAGEMENT DELEGATIONS AND RESPONSIBILITIES

The respective roles of the Council, Cabinet, GARMSC, the Section 151 officer, the Treasury Management Group the Treasury and Pension Fund Manager and the Treasury Team are summarised below. Further details are set out in the Treasury Management Practices.

### **Council**

Under the Constitution, the Council is responsible for “decisions relating to the control of the Council’s borrowing requirement.”

It agrees the annual Treasury Management Strategy Statement including Prudential Indicators, Minimum Revenue Provision Policy Statement and Annual Investment Strategy.

### **Cabinet**

Under the Constitution, the Cabinet “will exercise all of the local authority functions which are not the responsibility of any other part of the local authority, whether by law or under this Constitution.”

It considers and recommends to Council the annual Treasury Management Strategy Statement and receives a mid-year report and annual outturn report on Treasury Management activities.

### **Governance, Audit, Risk Management and Standards Committee**

GARMSC reviews the Treasury Management Strategy and monitors progress on treasury management in accordance with CIPFA codes of practice.

### **Director of Finance (Section 151 Officer)**

Under S151 of the Local Government Act 1972 the Council “shall make arrangements for the proper administration of their financial affairs and shall secure that one of their officers has responsibility for the administration of those affairs.” At Harrow, this responsibility is exercised by the Director of Finance.

The Director is responsible for implementing the policies agreed by the Council and Cabinet.

Under the Local Government Finance Act 1988 and the Local Government Act 2003 the Director also has responsibilities in respect of budget arrangements and the adequacy of resources. In terms of Treasury Management this means that the financing costs of the Capital Programme are built into the Revenue Budget as are any assumptions on investment income.

The Director chairs the Treasury Management Group and agrees major treasury management decisions, specifically including any borrowing decisions, delegated to officers.

### **Treasury Management Group**

Comprises Director of Finance, Head of Strategic and Technical Finance (Deputy S151 Officer), Treasury and Pension Fund Manager, Senior Finance Officer and is responsible for:

- Monitoring treasury management activity against approved strategy, policy, practices and market conditions;
- Ensuring that capital expenditure plans are continually reviewed in line with budget assumptions throughout the year to forecast when borrowing will be required.
- Approving changes to treasury management practices and procedures;
- Reviewing the performance of the treasury management function using benchmarking data on borrowing and investment provided by the Treasury Management Adviser (Capita Asset Services);
- Monitoring the performance of the appointed Treasury Management Adviser and recommending any necessary actions
- Ensuring the adequacy of treasury management resources and skills and the effective division of responsibilities within the treasury management function;
- Monitoring the adequacy of internal audit reviews and the implementation of audit recommendations

### **Treasury and Pensions Manager**

Responsible for the execution and administration of treasury management decisions, acting in accordance with the Council's Treasury Management Strategy Statement and CIPFA's "Standard of Professional Practice on Treasury Management"

### **Treasury Team**

Headed by Senior Finance Officer with responsibility for day-to-day treasury and investment and borrowing activity in accordance with approved Strategy, policy, practices and procedures and for recommending changes to the Treasury Management Group

## Counterparties

As agreed by Cabinet on 16 February 2017 the Council's criteria for an institution to become counterparty are:

### Specified Investments

These are sterling investments of a maturity period of not more than 364 days, or those which could be for a longer period but where the lender has the right to be repaid within 364 days if it wishes. These are low risk assets where the possibility of loss of principal or investment income is negligible. The instruments and credit criteria to be used are set out in the table below.

**Table 10 Specified Investments**

<b>Instrument</b>	<b>Minimum Credit Criteria</b>	<b>Use</b>
Debt Management Agency Deposit Facility	Government backed	In-house
Term deposits – other LAs	Local Authority issue	In-house
Term deposits – banks and building societies	AA- Long Term F1+Short-term 2 Support UK or AAA Sovereign	In-house
Money Market Funds	AAA	In-house

### Non-Specified Investments

Non-specified investments are any other type of investment (i.e. not defined as Specified above). They normally offer the prospect of higher returns but carry a higher risk. The identification and rationale supporting the selection of these other investments are set out in the table below.

**Table 11 Non - Specified Investments**

	<b>Minimum Credit Criteria</b>	<b>Use</b>	<b>Max total investment</b>	<b>Max. maturity period</b>
Term deposits – banks and building societies (excluding Lloyds / HBOS)	A Long Term F1 Short-term UK or AAA Sovereign	In-house	50%	3 months
Lloyds / HBOS	A Long Term F1 Short-term	In-house	50%	6 months
Callable Deposits	A Long Term F1 Short term	In-house	20%	3 months
UK nationalised Banks [RBS]	F2 Short-term	In-house	60%	36 months
Enhanced Cash Funds	AAA	In-house	25% (maximum £10 million per fund)	Minimum monthly redemption
Corporate bonds pooled funds, other non-standard investments and gilts		In house	£10m in total	Dependent on specific agreement
HB Public Law Ltd		In house	£0.1m	36 months

	<b>Minimum Credit Criteria</b>	<b>Use</b>	<b>Max total investment</b>	<b>Max. maturity period</b>
Investment Property Strategy *		In house	£20.0m	Dependent on specific agreement
Concilium Business Services Ltd t/a Smart Lettings Ltd		In house	£0.274m	36 months
Concilium Group Startup capital		In house	£0.702m	60 months
Concilium Group 5% Long Term Investment		In house	£1.5m	Dependent on specific agreement
Cultura London re Harrow Arts Centre		In house	£1m	25 years
Housing Development Vehicle (LLP) – Initially on acquisition of 100 homes		In house	£30m	Dependent on specific agreement

\*Investment to date totals £5.3m

## PRUDENTIAL INDICATORS 2017/18 OUTTURN

### Capital Expenditure and Funding

The Council undertakes capital expenditure on long-term assets. These activities may either be:

- Financed immediately through the application of capital or revenue resources (capital receipts, capital grants, revenue contributions etc.), which has no resultant impact on the Council's borrowing need; or
- If insufficient financing is available, or a decision is taken not to apply resources, the capital expenditure will give rise to a borrowing need.

The actual capital expenditure forms one of the required prudential indicators. The table below shows the actual capital expenditure and how this was financed.

**Table 1: Actual Capital Expenditure**

	2016/17	2017/18	2017/18
General Fund	Actual	Revised Budget	Actual
	£'000	£'000	£'000
<b>Expenditure</b>	<b>78,148</b>	<b>168,795</b>	<b>82,254</b>
<b>Funding:</b>			
Grants	22,160	21,187	13,309
Capital Receipts			6,403
Revenue Financing		69	487
Section 106 / Section 20 contributions	401	5,732	5,056
<b>TOTAL</b>	<b>22,561</b>	<b>26,988</b>	<b>25,255</b>
<b>Net financing need for the year</b>	<b>55,587</b>	<b>141,807</b>	<b>56,999</b>

	2016/17	2017/18	2017/18
HRA	Actual	Revised Budget	Actual
	£'000	£'000	£'000
<b>Expenditure</b>	<b>11,603</b>	<b>32,457</b>	<b>11,877</b>
<b>Funding:</b>			
Grants	48		
Capital Receipts	3,013	17,674	1,734
Revenue Financing	7,287	12,293	8,266
Section 106 / Section 20 contributions	1,255	314	400
<b>TOTAL</b>	<b>11,603</b>	<b>30,281</b>	<b>10,400</b>
<b>Net financing need for the year</b>	<b>0</b>	<b>2,176</b>	<b>1,477</b>



The funding excludes the Minimum Revenue Provision (depreciation on General Fund assets) which offsets the need for external borrowing. Further detail and explanations are contained within the Revenue and Capital Outturn report.

From an affordability perspective, which is the treasury consideration, the increase in expenditure has impacted on interest income. Almost all of the Housing Revenue Account's (HRA's) capital expenditure of £11.6m is funded from revenue sources and capital receipts.

### Overall Borrowing Need

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the 2016/17 unfinanced capital expenditure (see above table), and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through borrowing from external bodies (such as the Government, through the Public Works Loan Board [PWLB] or the money markets), or utilising temporary cash resources within the Council.

**Reducing the CFR** – the Council's (non-HRA) underlying borrowing need (CFR) is not allowed to rise indefinitely. Statutory controls are in place to ensure that capital assets are broadly charged to revenue over the life of the asset. The Council is required to make an annual revenue charge, called the Minimum Revenue Provision (MRP), to reduce the CFR. This is effectively a repayment of the non-HRA borrowing need (there is no statutory requirement to reduce the HRA CFR). This differs from the treasury management arrangements which ensure that cash is available to meet capital commitments. External debt can also be borrowed or repaid at any time, but this does not change the CFR.

The total CFR can also be reduced by:

- the application of additional capital financing resources (such as unapplied capital receipts); or
- charging more than the statutory revenue charge (MRP) each year through a Voluntary Revenue Provision (VRP).

The Council's 2016/17 MRP Policy (as required by CLG Guidance) was approved as part of the Treasury Management Strategy Report for 2016/17 on 18 February 2016.

The Council's CFR for the year is shown below, and represents a key prudential indicator. It includes PFI and leasing schemes on the balance sheet, which increase the Council's borrowing need. No borrowing is actually required against these schemes as a borrowing facility is included in the contract.

**Table 2: Capital Financing Requirement**

	2016/17	2017/18	2017/18
	Actual	Estimate	Actual
	£'000	£'000	£'000
<b>Capital Financing Requirement as at 31 March</b>			
Non – HRA	303,652	425,887	343,209
HRA	149,537	154,701	151,014
<b>TOTAL</b>	<b>453,189</b>	<b>580,588</b>	<b>494,223</b>
<b>Annual change in CFR</b>			
Non – HRA	40,086	122,235	39,557
HRA	0	5,164	1,477
<b>TOTAL</b>	<b>40,086</b>	<b>127,399</b>	<b>41,034</b>

**Reasons for annual change**

	2016/17	2017/18	2017/18
	Actual	Estimate	Actual
	£'000	£'000	£'000
Capital Expenditure	89,751	201,252	94,131
Non Borrowing sources of funding	-34,164	-57,269	-35,655
Minimum Revenue Provision	-15,501	-16,584	-17,442
<b>TOTAL</b>	<b>40,086</b>	<b>127,399</b>	<b>41,034</b>

The CFR value is greater than the outstanding borrowing (including finance leases) of £341.9m, indicating the level of cash generated by revenue balances.

Borrowing activity is constrained by prudential indicators for net borrowing and the CFR, and by the authorised limit.

**Gross borrowing and the CFR** - in order to ensure that borrowing levels are prudent over the medium term and 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 (2016/17) plus the estimates of any additional capital financing requirement for the current (2017/18) and next two financial years. This essentially means that the Council is not borrowing to support revenue expenditure. The table below highlights the Council's gross borrowing position against the CFR. The Council has complied with this prudential indicator.

**Table 3: Borrowing**

	2016/17	2017/18	2017/18
	Actual	Estimate	Actual
	£'000	£'000	£'000
<b>Capital Financing Requirement</b>	453,189	580,588	494,223
<b>Gross borrowing</b>	351,466	350,434	341,918
<b>Under borrowing</b>	<b>101,723</b>	<b>230,154</b>	<b>152,305</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. The table below demonstrates that during 2017/18 the Council has maintained gross borrowing within its authorised limit.

**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.

**Table 4: Boundaries**

	2016/17	2017/18
	£m	£m
<b>Authorised Limit for external debt</b>		
Borrowing and finance leases	469	568
<b>Operational Boundary for external debt</b>		
Borrowing	334	448
Other long term liabilities	16	16
<b>Total</b>	350	464
<b>Upper limit for fixed interest rate exposure</b>		
Net principal re fixed rate borrowing	334	448
<b>Upper limit for variable rate exposure</b>		
Net principal re variable rate borrowing	0	0
Upper limit for principal sums invested over 364 days	60	60

The approved operational boundary for debt is based on actual debt at the start of the year plus the actual borrowing requirement for the net projected capital expenditure in the year. The authorised limit is based on CFR balances. Total borrowing has been within both limits during the year.

**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 5 - Ratio of Financing Costs to Revenue Stream**

	2016/17	2017/18	2017/18
	Actual	Approved	Actual
	%	%	%
<b>Ratio of financing costs to net revenue stream</b>			
Non - HRA	14.2	15.4	14.7
HRA Including depreciation	40.4	43.1	40.4

This indicator identifies the trend in the cost of capital (depreciation, impairments, borrowing and other long term obligation costs net of investment income) against the net revenue stream.

**Table 6 - Incremental Impact of Capital Investment Decisions (excluding Regeneration)**

	2016/17	2017/18	2017/18
	Actual	Approved	Actual
	£	£	£
<b>Incremental impact of capital investment decisions</b>			
Increase in Council Tax (Band D) per annum	38.98	63.21	37.51

This indicator identifies the revenue costs associated with the proposed capital programme and the impact on Council Tax.