Scrutiny of the Treasury Management Strategy and Policies – Questions and Answers (Overview and Scrutiny Committee 18 January 2021)

The following questions and answers will help to demonstrate that the Council's Treasury Management Strategy and Policies were subject to robust member scrutiny and demonstrate compliance with the CIPFA Code of Practice for Treasury Management.

First some questions on the day to day process.

Question No. 1

On a daily basis, how do you work out whether we need to borrow money or have spare cash available that we can lend out?

Cash flow projections are prepared annually and daily. The annual cash flow projections are prepared from the previous years' cash flow records, adjusted for known changes in levels of income and expenditure and also changes in payments and receipts dates. These details are supplemented on an ongoing basis by information received on new or revised amounts to be paid or received as and when they are known and the council downloads data from its bank on a daily basis.

Question No. 2

If I have understood this correctly, in essence you are estimating what you expect the end of day position to be at the bank when all the pending transactions, including payments to suppliers and the clearance of cheques or direct debits into our account, have been processed – what happens therefore if you get it wrong?

Of course, from time-to-time we receive amounts earlier or later than expected, amounts we weren't expecting or where values differ from those reported to us. This can be for a number of reasons e.g. new burdens funding, payments made to us in error (for instance intended for Wyre Forest or LCC) or emergency funding at short notice (e.g. Covid related).

With the introduction of a group aggregate auto transfer facility ('roll-up') in February 2018, any funds remaining in the council's bank accounts at close of business are automatically cleared into the interest bearing Liquidity account thus stopping any under investment of funds. There will be an automatic transfer from the interest bearing account (assuming adequate funds available) crediting the group control account with the required balance from the interest bearing account. This avoids an overdrawn balance and the subsequent charges.

From 1 September 2011, and following a cost/benefit analysis, we took a decision to cease the formal overdraft facility. The formal overdraft facility used to cost the council £2,000 plus 1% over the base rate for overdrawn net balances over £500,000. The new arrangement now incurs charges at 4% over the current base rate for net overdrawn balances with no annual arrangement fee. There have been no occasions since the introduction of the new group aggregate transfer facility when the council's net bank account position was overdrawn.

Question No. 3

Is there one person who does the day to day dealing and what happens if they are away on leave?

Within the Treasury Management Policy Statement and Practices that is approved annually by Cabinet/Council in March/April there is a list of all the different functions and a table showing which officers can do what. For example, the day to day dealing can be done by, either of the three Senior Account Managers (Penny Jones, Joanne McCaffery – one PT post is vacant) and either of the two Account Managers (Louise Rowland and Clare Riche). Authorisation of short term borrowing or investing falls to the Corporate Director Resources (Clare James), Head of Finance (Veronica Wilson), the Head of the Contact Centre (Peter Mason), the Head of Governance (Joanne Billington), the Head of Business Support (Liesl Hadgraft) or the Legal Services Manager (Mary Grimshaw).

Question No. 4

So what do you have to do if you want to invest some money?

The Treasury Management Policy Statement and Practices states that the council applies the creditworthiness service provided by Link Asset Services who are our Treasury Management Consultants. This service employs a sophisticated modelling approach combining credit ratings, credit watches and credit outlooks (see Appendix 1) in a weighted scoring system which is then combined with an overlay of CDS (Credit Default Swaps) spreads for which the end product is a series of colour coded bands which indicate the relative creditworthiness of counterparties. They provide us with this weekly credit list and supplement it with emails for any changes to counterparty credit ratings. Lending is only made to counterparties within the council defined colour bands according to the colour coded creditworthiness list.

In addition, the Practices say that the council will also look at other market information in order to establish a full investment strategy; such as up to date market information, which includes Sovereign and individual counterparty ratings, together with a wide range of relevant economic data. In reality, other than day to day news headlines/reports, no further challenges are made to the treasury advisors guidance.

If we are using the council's bank, the NatWest, for investments in the Liquidity account the balance is left in the current account and will be automatically transferred into the Liquidity account at the close of business. If we are using the Money Market Funds then this is entered on to the SunGard System and an email is sent prompting the authorising officer to agree the transfer. All transactions on the SunGard System must be authorised before, either 1pm. 1.30pm or 2pm dependent on the fund, in order for them to be actioned that day

If we are using the Bank of Scotland or Nationwide we ring up to obtain the rate for the amount and length of time we want to invest and using this information we complete a temporary lending form detailing the amount to be invested, the interest rate and the term. Once this form is authorised we phone the Bank of Scotland or Nationwide back to confirm the deal and give notice if necessary and a bank transfer is made from the council's banks. If we are using Svenska Handelsbanken, Qatar National Bank or Santander again a temporary lending form is completed and once authorised a bank transfer is made from the council's bank.

Question No. 5

What about if you need to borrow money – what happens then?

The Treasury Management Policy Statement and Practices clearly states that the council must access temporary loans through approved brokers on the London money market. The approved borrowing limit for short term debt has been set at £13.459m in 2020/21.

In essence, we telephone the brokers and ask them to find somebody who can lend us the amount we need and for the required term, for example, are we happy for the money to be called back at any time or do we want to fix it to a particular date. We aren't fussy about who lends us the money and the brokers currently charge commission at 1% of interest due. There is no commission charge for undertaking investment transactions via the brokers.

The last time we borrowed via the brokers was back in 2009/10.

Question No. 6

So what guarantees do we have that somebody in the finance team isn't going to disappear to the Caribbean with a significant amount of the council's money – presumably there are sufficient checks and balances?

Firstly, I'm not good in places with extreme temperatures but on a more serious note, there are a number of controls in place including;

- ✓ All lending is only made to institutions on the Link Creditworthiness Weekly List.
- ✓ All loans raised and repayments made go directly to and from the institution's bank account.
- ✓ Authorisation limits are set for every institution.
- ✓ Brokers have a list of named officials authorised to perform loan transactions.
- ✓ There is adequate insurance cover for employees involved in loan management and accounting.
- ✓ The control totals for borrowing and lending are regularly reconciled with the ledger balance sheet codes by the Financial Services Team.
- ✓ There is a separation of duties in the Section between the processing and authorisation of transactions.
- ✓ The council's bank holds a list of council officials who are authorised signatories.
- ✓ No member of the Treasury Management team responsible for borrowing and lending is an authorised signatory.

A key aim of the Treasury Management Policy Statement is that 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. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

And if you are still worried, then it is worth noting that the council has 'Fidelity' insurance cover with Zurich Municipal (ZM). This covers the loss of cash by fraud or dishonesty of employees. This cover is limited per transaction as follows:

- ✓ 13 designated officers (Corporate Director of Resources, Head of Contact Centre, Head of Governance, Head of Business Support, Legal Services Manager, Head of Finance,

Principal Accountant, Senior Account Manager x 3, Financial Systems and Payments Officer and Financial Service Officer x 2 are indemnified for £3m.
- ✓ All other employees are indemnified for £250,000.

Question No. 7

How do you know if you are doing a good job – what measures do you use to assess your performance?

We do an annual report in June/July each year showing the overall position and activities for the previous year. The report includes the following issues, where relevant:

- ✓ total debt and investments at the beginning and end of the financial year and average interest rates;
- ✓ borrowing strategy for the year compared to actual strategy, including interest paid;
- ✓ investment strategy for the year compared to actual strategy, including interest received;
- ✓ explanations for variance between original strategies;
- ✓ debt rescheduling done in the year;
- ✓ actual borrowing and investment rates achieved through the year;
- ✓ comparison of return on investments to the benchmark 7-day LIBID rate (London Interbank Bid Rate); and
- ✓ compliance with Prudential and Treasury Indicators.

We also complete a half yearly Report on Treasury Management which is submitted to Council in November/December which reviews the performance of the debt and investment portfolios. This report contains the same information as the annual report but only includes information for the first 6 months of the year.

Last year investments earned an average return of 0.87% against a benchmark LIBID (London Interbank Bid Rate) 7-day average of 0.53% whilst the Bank of England base rate stated the year at 0.75% and reduced to 0.25 and then 0.10% in March for the remainder of the year.

In the six months to 30 September 2020 investments have achieved an average return of 0.44% against a benchmark LIBID 7-day average of 0.41%.

And now just a couple of other questions concerning the wider Treasury Management arrangements…

Question No. 8

I understand that we are with the NatWest bank and have been for some time – do we ever consider switching?

Whilst we have been with NatWest for nearly 30 years, banking services have traditionally been re-tendered or renegotiated every 3 years to ensure that the level of prices reflect efficiency savings achieved by the supplier and current pricing trends. The council retendered for Banking Services using the Government Framework in 2016. This resulted with our present providers NatWest being awarded the contract which resulted in considerable savings for the Authority. We have exercised our contract extension option and the Natwest are currently working on revised contract prices which we can then use to determine whether we benchmark or go out to tender next year.

Question No. 9

And whilst we are talking about the costs of treasury management – do we have other advisors that we use and how much do they cost?

When the council lost its debt free status during 2007/08 Link Asset Services was engaged as the council's treasury advisor. The initial appointment was for one year and was considered to be value for money having sought other quotations. The service was benchmarked in 2016 and further benchmarking exercises will be conducted every three years to ensure value for money is maintained. The cost of the service is £7,750 per year and training is available for staff and members within this price.

Question No. 10

I know you've mentioned the half yearly and annual performance reports to Council but are there other reports that we need to produce to ensure compliance with the CIPFA Code of Practice for Treasury Management?

Yes, there are a number of reports that we are required to complete and take to Council on an annual basis. It is a requirement as well as being useful to review the Treasury Management Policy Statement and Treasury Management Practices each year. The specific requirements ask for the following:

- ✓ The Treasury Management Strategy Statement - sets out the specific expected treasury activities for the forthcoming financial year and is submitted to the Cabinet in March and then full Council in April. It involves determining the appropriate borrowing and investment decisions in the light of the anticipated movement in both fixed and shorter-term variable interest rates. For instance, the council may decide to postpone borrowing if fixed interest rates are expected to fall, or borrow early if fixed interest rates are expected to rise. It covers a number of items including:

- Prudential and Treasury Indicators
- current Treasury portfolio position
- borrowing requirement
- prospects for interest rates
- borrowing strategy
- policy on borrowing in advance of need
- debt rescheduling
- investment strategy
- creditworthiness policy
- policy on the use of external service providers
- any extraordinary treasury issue
- the MRP strategy

- ✓ The Annual Investment Strategy – is received at the same time as the Treasury Management Strategy Statement and sets out the following:

- The council's risk appetite in respect of security, liquidity and optimum performance
- The definition of 'high credit quality' to determine what are specified investments as distinct from non- specified investments
- Which specified and non-specified instruments the council will use
- Whether they will be used by the in house team, external managers or both (if applicable)
- The council's policy on the use of credit ratings and other credit risk analysis techniques to determine creditworthy counterparties for its approved lending list
- Which credit rating agencies the council will use
- How the council will deal with changes in ratings, rating watches and rating outlooks
- Limits for individual counterparties and group limits
- Country limits
- Cash balances
- Interest rate outlook
- Budgeted investment return
- Use of a cash fund manager (if applicable)
- Policy on the use of external service providers (if applicable)

✓ The Annual Minimum Revenue Provision Statement - is received at the same time as the Treasury Management Strategy Statement and sets out how the council will make revenue provision for repayment of its borrowing using the four options for so doing. Our adopted policy is that all expenditure reflected within the debt liability at 31 March 2008 will under delegated powers be charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method (Asset Life Method).

✓ Policy on Prudential and Treasury Indicators – the limits are approved by Council before the beginning of each financial year and, in addition to being presented with the Revenue and Capital Estimates in March, are incorporated into the Annual Treasury Management Strategy.

✓ A Capital Strategy will be prepared each year for approval by Cabinet in March. This is a recent requirement introduced in response to some of the more risky investments undertaken by local authorities in response to falling budgets. Ours will be fairly basic compared to those authorities with significant external borrowing and complex loans and will evolve as new guidance is issued.

<u>Question No. 11</u>

I'm interested in what our advisors said about the prospects for interest rates?

The advisors most recent forecasts indicated for the Treasury Management Activity Report to September 2020 that the base rate would not rise from its position of 0.10% until at least March 2023. However, much is dependent on the current global pandemic as well as the impact of Brexit.

<u>Question No. 12</u>

And if we wanted to borrow to fund some of the capital works that are currently being assessed, what would the costs be?

If we borrowed £2m in March 2021 the interest rate is currently projected to be 2% (PWLB) and if we used the money to fund assets with lives of 25 years then the cost for principal and interest repayments would be £120,000pa.

We currently have debt of £1.552m and incur debt charges of £164,389 – this isn't expected to fall until 2024/25 when the assets with a 15 year life span drop out of the MRP calculation.

The Prudential Code for Capital Finance aims to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable. The Code sets out indicators that must be used and requires local authorities to set relevant limits and ratios. As the council is currently projecting a gap between expenditure and income of £2.6m in 2024/25 further borrowing is not considered to be affordable, prudent or sustainable.

And finally, if there are any burning issues that we haven't addressed or any further questions, please feel free to do so now.