Police and Crime Commissioner North Yorkshire

Appendix C1

Report of the Chief Finance Officer of the PCC to the Police and Crime Commissioner

24th February 2015
Status: For Decision

Treasury Management and Prudential Indicators 2015/18

1. Purpose

To comply with the CIPFA Prudential Code of Practice, the PCC is required to set a range of Prudential Indicators for the financial year 2015/16. The code states that Prudential Indicators for Treasury Management should be considered together with the Annual Investment Strategy for 2015/16. The content of this report addresses this requirement.

2. Recommendations

The PCC is asked to:

2.1 Approve the Prudential Indicators appended to this report.

2.2 Approve the Annual Investment Strategy set out at Appendix A.

2.3 Note that future investments will be placed in line with the strategy in Appendix A.

3. Reasons

3.1 Prudential Indicators

The Prudential Code requires authorities (including the PCC) to self regulate the affordability, prudence and sustainability of their capital expenditure and borrowing plans, by setting estimates and limits, and by publishing actuals, for a range of Prudential Indicators. It also requires them to ensure their Treasury Management Practices are in accordance with good practice.

3.2 The Code imposes on authorities clear governance procedures for setting and revising of Prudential Indicators, and describes the matters to which an authority will have regard when doing so. This is designed to deliver accountability in taking capital financing, borrowing and Treasury Management decisions. A fundamental provision of the Prudential Code is that over the medium term net borrowing will only be for a capital purpose.

3.3 Under the Code, individual authorities are responsible for deciding the level of their affordable borrowing, having regard to the code. Under the code The PCC is required to set a range of Prudential Indicators for the financial year 2015/16.

3.4 The code states that Prudential Indicators for Treasury Management should be considered together with the Annual Investment Strategy.

3.5 Affordability

The following indicators are required to assess the affordability of the capital investment plans. They provide an indication of the impact of the capital investment plans on overall PCC finances.

3.5.1 Ratio of Financing Costs to Net Revenue Stream

This indicator identifies the trend in the cost of capital against the net budgetary requirement. In effect it is looking at how much of the revenue budget needs to be set aside for the funding of capital decisions and how sustainable this is going forward.

At this stage the PCC doesn’t have any plans to borrow to fund capital expenditure and this ratio only takes into account the financing costs of capital. Therefore the percentages shown in the attachment are very small and in the period 2015/16 to 2017/18, when the current plan includes no borrowing, then there is a small net benefit to the organisation in terms of interest receivable.

The PCC is aware that the vast majority of Capital Expenditure is funded from revenue contributions to Capital, if these were taken in account then around 3% to 4% of the net budget requirement is being set aside each year to fund capital.

3.5.2 *Incremental Impact of Capital Investment Decisions on Band D Council Tax*

This indicator shows the incremental impact of the additional capital expenditure that is planned in the current programme on the Band D council tax.

Again the way that Capital is funded within North Yorkshire means that this ratio shows that there is a positive effect on the Band D from Capital Investment decisions.

Perhaps a more indicative way of looking at this is as follows:
In 2017/18 the plan assumes an increase in Precept of 1.99%, this would generate around £1.2m additional funding. Also in 2017/18 the contribution to the Capital Programme is expected to be £4.9m, which is £1.14m higher than the projected contribution in 2016/17.

If this was taken into account this ratio would show that nearly 100% of the projected precept increase in 2017/18 would be to fund the increased costs of supporting the capital programme.

3.6 Prudence

The 'prudence' indicator generally looks at the level of borrowing needed to maintain the current plans of the organisation. Based on current plans of no borrowing the Capital Plans of the organisation are very prudent as the percentage of Capital Expenditure to be funded by borrowing is zero.

If the current contributions from revenue were replaced by borrowing then this ratio would show the following level of the capital plan funded by borrowing:

- 2015/16 – 17%
- 2016/17 – 59%
- 2017/18 – 89%

3.6.1 *The PCC's Borrowing Need (The Capital Financing Requirement)*

The Capital Financing Requirement (CFR) measures the PCC's underlying need to borrow for Capital purposes and ensures that borrowing is only undertaken to fund capital assets and not support revenue expenditure.

The CFR as set out in the attachments are very small and because there is no borrowing the PCC can be assured that any borrowing that may be taken out in the future would not be to support revenue expenditure.

3.6.2 Limits to Borrowing Activity

Within the Prudential indicators there are a number of indicators to ensure that the PCC operates its activities within well defined limits.

For the first of these the PCC needs to ensure that its total borrowing net of any investments does not, except in the short term, exceed the total of the CFR in the preceding year plus the estimates of any additional CFR for 2015/16 and the following two financial years. This allows some flexibility for limited early borrowing for future years, to take advantage of market opportunities and to build in budget uncertainty.

The projected forecasts detailed in the attachment show that given the significant cash and investment balances that the PCC has there is no need, or scope, to borrow externally and instead the PCC would need to use internal funds, which is in effect internal borrowing, to fund capital expenditure going forward so as not to breach this indicator.

3.6.3 A further two prudential indicators control or anticipate the overall level of borrowing. These are:

- The ***Authorised Limit*** which represents the limit beyond which borrowing is prohibited and needs to be set and revised by the PCC, borrowing beyond this limit would be ultra vires.

- The ***Operational Boundary*** which is based on the probable external debt during the course of the year. It includes scope for borrowing for revenue purposes that may be required in the short term during the year, if for instance a large grant payment was delayed.

3.7 Treasury Management Indicators

The purpose of these is to contain the activity of the Treasury function within certain limits, thereby reducing the risk or likelihood of an adverse movement in interest rates or borrowing decisions impacting negatively on the PCC's overall financial position.

3.7.1 Upper Limits on Borrowing

This indicator identifies a maximum level of borrowing that can be made at Fixed and Variable interest rates.

This means that if the PCC did have to borrow that 50%-100% of our borrowing will be at rates fixed until the loan is repayable, while no more than 50% will be at variable rates so liable to change at short notice.

3.7.2 *Upper Limits on Investments*

This indicator identifies a maximum level of investments that can be made at Fixed and Variable interest rates.

This means 50%-100% of our investments will be at rates fixed until the investment matures, while no more than 50% will be at variable rates so liable to change at short notice.

3.7.3 *Maturity Structure of Debt*

These gross limits are set to reduce the PCC's exposure to large fixed rate sums falling due for re-financing within a short timeframe. Upper and lower limits are required which the PCC is asked to approve.

3.7.4 *Upper Limit for Sums Invested for a Period of over 364 days*

This indicator sets a limit on the level of investments that can be made for more than 364 days. The PCC currently does not provide approval to invest beyond a 1 year period. Given the large cash balances it should perhaps be reviewed as to whether better returns on investments could be achieved through longer term investment periods.

3.8 Annual Investment Strategy

The proposed Annual Investment Strategy for 2015/2016 is attached at Appendix A.

3.9 Returns on Investments

While returns on investments are of secondary importance to the security of the sums invested, it is still important to consider the potential impact of approving the Investment Strategy put forward. The limited number of counterparties on our list potentially restricts the returns, in the form of interest receivable, which the PCC can make.

3.10 Given the current low level of interest rates, the Bank of England Base rate is currently 0.5% and has been for almost 6 years, the impact will be relatively small. The budget set for interest receivable in 2015/16 is just over £200k.

3.11 Counterparty Limits

As per the strategy in Appendix A, limits for specified counterparties are:

Institution	Sector Rating	Limit
Lloyds TSB Bank Plc	B - 12 months	8,750,000
Bank of Scotland Plc	B - 12 months	
The Royal Bank of Scotland Plc	B - 12 months	8,750,000
National Westminster Bank Plc	B - 12 months	

HSBC Bank plc	G - 3 months	8,750,000
Barclays Bank plc	G - 3 months	8,750,000
Nationwide BS	G - 3 months	8,750,000
Debt Management Office	Y - 12 months	10,000,000

4. Implications

4.1 Finance
There are no financial implications arising from this report that is not included above.

4.2 Diversity & Equal Opportunities
There are no issues arising from this report to bring to the PCC's attention.

4.3 Human Rights Act
There are no Human Rights Act implications arising from this report.

4.4 Sustainability
This report is part of the process to establish sustainable annual and medium term financial plans and maintain prudent financial management.

4.5 Risk
The investment strategy put forward today seeks to minimise the risks of the PCC while ensuring that the cash balances of the PCC are managed in line with proper practice and to ensure funds are available to make payments at the correct time.

5. Conclusions

5.1 To comply with the CIPFA Prudential Code of Practice the PCC is required to set a range of Prudential Indicators for the financial year 2015/16.

5.2 The CIPFA code does not set benchmark indicators. Each organisation must use its judgement when setting indicators.

5.3 Based on the indicators proposed above, the revenue budget, capital programme and associated financing are within prudent limits.

5.4 A prudent Investment Strategy has been put forward for approval that seeks to firstly secure the money being invested before secondly looking at rates of return.

Michael Porter
CFO for the PCC

APPENDIX A

Annual Investment Strategy

1. The Commissioner will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code"). The Commissioner's investment priorities are:

- the security of capital; and
- the liquidity of its investments.

2. The Commissioner will also aim to achieve the optimum return on investments commensurate with proper levels of security and liquidity. The Commissioner's risk appetite is low in order to give priority to security of investments.

3. The borrowing of monies purely to invest or on-lend and make a return is unlawful and the Commissioner will not engage in such activity.

4. Investment instruments are identified as either 'Specified' or 'Non-Specified' Investments. The Commissioner's available instruments are listed in paragraph below. Counterparty limits will be as set through the Treasury Management Practices.

5. It is proposed that the Annual Investment Strategy for 2015/16 is based solely upon the use of "specified" investments listed below, with all such investments being sterling denominated, with maturities up to a maximum of 364 days (<12 months) meeting the minimum "high" credit rating where applicable:

- Debt Management Agency Deposit Facility
- Term Deposits - UK Government
- Term Deposits - other local authorities
- Term Deposits - banks and building societies
- Money market funds

6. A summary of the current investment periods are outlined below with the main emphasis being on increasing the liquidity of funds by reducing the length of time any one investment should be held with a counterparty:

Sector Colour Code	Current Investment period
Green	3 months
Red	6 months
Orange	12 months
Blue	12 months (Government Backed)
Purple	12 months
Yellow	12 months

7. The Treasury Management Function takes cognisance of latest market information produced by the treasury advisors (Sector) to support decisions regarding maturity periods and counterparty limits.

Due the current economic climate presenting significant difficulties for the treasury management function to find available counterparty's changes were made to the approved list of counterparties. The current limits are shown below:

Institution	Sector Rating	Limit
Lloyds TSB Bank Plc	B - 12 months	8,750,000
Bank of Scotland Plc	B - 12 months	
The Royal Bank of Scotland Plc	B - 12 months	8,750,000
National Westminster Bank Plc	B - 12 months	
HSBC Bank plc	G - 3 months	8,750,000
Barclays Bank plc	G - 3 months	8,750,000
Nationwide BS	G - 3 months	8,750,000
Debt Management Office	Y - 12 months	10,000,000