WARWICK DISTRICT COUNCIL	Executive 20 May 2020	Agenda Item No. **10(C)**

Title	Treasury Management Strategy 2020/21
For further information about this report please contact	Richard Wilson, Principal Accountant (Capital & Treasury) 01926 456801 or email richard.wilson@warwickdc.gov.uk
Wards of the District directly affected	N/A
Is the report private and confidential and not for publication by virtue of a paragraph of schedule 12A of the Local Government Act 1972, following the Local Government (Access to Information) (Variation) Order 2006?	No
Date and meeting when issue was last considered and relevant minute number	N/A
Background Papers	Treasury Management Information via External Advisers, Brokers, External Investment Agents etc.

Contrary to the policy framework:	No
Contrary to the budgetary framework:	No
Key Decision?	Yes
Included within the Forward Plan? (If yes include reference number)	Yes Ref # 1116
Equality Impact Assessment Undertaken	No – not relevant

Officer/Councillor Approval		
Officer Approval	**Date**	**Name**
Chief Executive/Deputy Chief Executive	3/3/20	Andrew Jones
Head of Service	19/2/20	Mike Snow
CMT		
Section 151 Officer	19/2/20	Mike Snow
Monitoring Officer	3/3/20	Andrew Jones
Finance	18/2/20	Richard Wilson
Portfolio Holder(s)	5/3/20	Cllr Richard Hales
Consultation & Community Engagement		
None		
Final Decision?		Yes
Suggested next steps (if not final decision please set out below)		

1. Summary

1.1. This report details the strategy that the Council will follow in carrying out its treasury management activities in 2020/21.

1.2. Activities in pursuance of the Climate Emergency declaration will inform and direct the treasury management function until at least 2024/25.

2. Recommendation

2.1. That Council ratifies the decision of the Chairman of the Council and Group Leaders on 25 March 2020:

a) The Treasury Management Strategy for 2020/21 as outlined in paragraph 3.2 and contained in Appendix A,

b) The 2020/21 Annual Investment Strategy as outlined in paragraphs 3.3 and contained in Appendix B including the following changes:

   1. That the Council divests from funds that contain direct ownership of fossil fuel extraction companies, or commingled funds that include fossil fuel public equities and corporate bonds, by no later than the end of 2025, and ideally by the end of 2022, as outlined in paragraph 3.7.

   2. That a separate non-Treasury Management 'Investment Regeneration Strategy' is brought to the Executive during the first quarter of 2020/21.

c) The Minimum Revenue Provision Policy Statement as outlined in paragraph 3.5 and contained in paragraphs 5.1 to 5.4 of Appendix C.

d) The Prudential Indicators as outlined in paragraph 3.6 and contained in Appendix D.

3. Reasons for the Recommendations

3.1. The Council's treasury management operations are governed by various Treasury Management Practices (TMPs) that the CIPFA Treasury Management Code requires be produced by the Council and adhered to by those officers engaged in the treasury management function. These TMPs have previously been reported to the Executive and are subject to periodic Internal Audit review.

3.2. There have been two changes to the TMPs, as outlined below, which is effectively one change that impacts on two TMPs:

TMP 1 – Risk management

Paragraph 3.5 – Adjusted to reflect the impact of the risk-based audit approach required by the Internal Audit Charter.

TMP 7 – Budgeting, accounting and audit arrangements

Paragraph 2.1 – Adjusted to reflect the impact of the risk-based audit approach required by the Internal Audit Charter.

3.3. Under CIPFA's updated *Treasury Management in Public Services Code of Practice* the Council continues to be required to have an approved annual *Treasury Management Strategy*, under which its treasury management operations can be carried out. The proposed Strategy for 2020/21 is included as Appendix A.

3.4. This Council has regard to the Government's Guidance on Local Government Investments. The guidance states that an *Annual Investment Strategy* must be produced in advance of the year to which it relates and must be approved by the full Council. The Strategy can be amended at any time and it must be made available to the public. The *Annual Investment Strategy* for 2020/21 is shown as Appendix B.

3.5. The Council has to make provision for the repayment of its outstanding long-term debt and other forms of long-term borrowing such as finance leases. Statutory guidance issued by MHCLG requires that a statement on the Council's *Minimum Revenue Provision (MRP) Policy* should be submitted to full Council for approval before the start of the relevant financial year. This is contained in Appendix C.

3.6. The *Prudential Code for Capital Finance in Local Authorities* was last revised in 2018 and introduced new requirements for the way that capital spending plans are considered and approved, in conjunction with the development of an integrated Treasury Management Strategy. The Prudential Code requires full Council to approve a number of Prudential Indicators, set out in Appendix D, which must be considered when determining the Council's Treasury Management Strategy for a minimum of the next three financial years.

3.7. The Executive requested that this Treasury Management Strategy Statement consider the policy of investing in fossil fuels. The investments over which the Council has any direct control of investments to fossil fuel extraction companies are the two corporate equity funds. By the nature of the existing pooled funds they invest around 5-10% in fossil fuel companies and the Council is unable to elect to exclude this. Therefore, the recommendation is to divest from these two funds no later than the end of 2025, and ideally by the end of 2022. The earlier date for divestment will need to have regard to market conditions and the resources within the Finance Team. Subject to the immediate financial needs of the Council, this money would then be re-invested in non-carbon or ESG equity funds or alternative investments in-line with the Investment Strategy.

3.8 The Treasury Management Strategy had been due to be considered by Executive on 18 March with a view to them recommending it to Council on 25 March. After the Executive was cancelled the report was then moved to the 25 March Council, to reduce the need for Councillors to meet in light of the Coronavirus national health emergency. However, the 25 March Council meeting was also cancelled following tight controls on public movement. Therefore, to enable the Council to move forward and following legal advice, the Group Leaders and Chairman agreed to the decisions, subject to them being ratified by Council.

4. Policy Framework

4.1. Fit For the Future (FFF)

The Council's FFF Strategy is designed to deliver the Vision for the District of making it a Great Place to Live, Work and Visit and be carbon neutral by 2030. To that end amongst other things the FFF Strategy contains several Key projects.

The FFF Strategy has three strands – People, Services and Money and each has an external and internal element to it. The table below illustrates the impact of this proposal if any in relation to the Council's FFF Strategy.

FFF Strands		
People	**Services**	**Money**
External		
Health, Homes, Communities	**Green, Clean, Safe**	**Infrastructure, Enterprise, Employment**
<u>Intended outcomes:</u> Improved health for all. Housing needs for all met. Impressive cultural and sports activities. Cohesive and active communities.	<u>Intended outcomes:</u> Area has well looked after public spaces. All communities have access to decent open space. Improved air quality. Low levels of crime and ASB.	<u>Intended outcomes:</u> Dynamic and diverse local economy. Vibrant town centres. Improved performance / productivity of local economy. Increased employment and income levels.
Impacts of Proposal		
No direct impact	Potential impact from divesting in fossil fuel equities	No direct impact
Internal		
Effective Staff	**Maintain or Improve Services**	**Firm Financial Footing over the Longer Term**
<u>Intended outcomes:</u> All staff are properly trained. All staff have the appropriate tools. All staff are engaged, empowered and supported. The right people are in the right job with the right skills and right behaviours.	<u>Intended outcomes:</u> Focusing on our customers' needs. Continuously improve our processes. Increase the digital provision of services.	<u>Intended outcomes:</u> Better return / use of our assets. Full cost accounting. Continued cost management. Maximise income earning opportunities. Seek best value for money.
Impacts of Proposal		
No impact	No impact	To continue to maximize the income earned on our investments whilst first ensuring security and appropriate levels of liquidity.

4.2. Supporting Strategies

Each strand of the FFF Strategy has several supporting strategies. The Treasury Management function is consistent with the relevant supporting strategies.

4.3. Changes to Existing Policies

The Treasury Management function is in accordance with existing policies, save for the recommendation to divest from direct ownership of fossil fuels companies or commingled funds that include fossil fuel public equities and corporate bonds by no later than 2025, in pursuance of the Council's Climate Emergency Declaration.

4.4. The Council will be considering a *Investment Regeneration Strategy* during the early part of 2020/21, which may have an impact on the Council's increased use of non-specified investments.

4.5. Impact Assessments

There are no impacts of new or significant policy changes proposed in respect of equalities.

5. Budgetary Framework

5.1. The Treasury Management Strategy has a significant impact on the Council's budget through its objective of maximising investment income and minimising interest payable whilst ensuring the security and liquidity of financial resources.

The 2020/21 budget for investment income, after inclusion of growth items, is as follows:

2020/21 Budget	£'000
External investment income	693.3
Deferred capital receipts interest	17.7
Long-term debtor loans	233.6
less : HRA allocation	-436.5
Net interest to General Fund	508.1

5.2. Divesting from the current two equity funds and the re-procurement of suitable alternative funds will incur an additional cost. Any costs will be included in a future budget report, before a re-procurement.

6. Risk Management

6.1. Investing the Council's funds inevitably creates risk and the Treasury Management function effectively manages this risk through the application of the SLY principle. Security (S) ranks uppermost, followed by Liquidity (L) and finally Yield (Y). Social impact will be an underlining principle. It is accepted that longer duration investments increase the security risk within the portfolio; however this is inevitable in order to achieve the optimal return and still comply with the SLY principle which is a cornerstone of treasury management within local authorities.

6.2. Section 1 of Appendix B (the annual *Treasury Management Investment Strategy*) provides more detail on how the risk is mitigated.

6.3. The Council does not have a specific risk register for Treasury Management but it does feature within the Finance risk register.

6.4. By engaging with our treasury management consultants, Link Asset Services (Link), the Council is able to minimise the risks to which it is exposed. Link provide regular briefings, alerts and advice in respect of the Council's portfolio. They also provide training for Members and officers responsible for the Council's treasury management function, to ensure they are informed and competent.

6.5. The strategies outlined in this report are based on an orderly exit from the European Union at the end of December 2020, with a trade deal. There is significant risk to counterparty creditworthiness, interest rate assumptions and the economic should a trade deal not be agreed by that date. The treasury management function will keep this under review, and bring forward modified strategies for approval should the need arise.

7. Alternative Option(s) considered

7.1. An alternative to the strategy being proposed for 2020/21 would be to not alter the current strategy to invest without specific reference to any Environmental, Social and Governance (ESG) issues. Keeping the existing equity funds, which invest in fossil fuels, may provide higher returns than the alternative of divesting these funds and investing in non-carbon or ESG equity funds.

8. Background

8.1. The Council is required to operate a balanced budget, which broadly means that cash raised during the year will meet cash expenditure. Part of the treasury management operation is to ensure that this cash flow is adequately planned, with cash being available when it is needed. Surplus monies are invested in low risk counterparties or instruments commensurate with the Council's low risk appetite, providing adequate liquidity initially before considering investment return (i.e. Security, Liquidity, Yield).

8.2. The second main function of the treasury management service is the funding of the capital plans, which provide a guide to the Council's overall borrowing requirement. This is longer-term cash flow planning, to ensure that the Council can meet its capital spending obligations. This management of longer-term cash may involve arranging long or short-term loans, or using longer-term cash flow surpluses. On occasion, when it is prudent and economic, any debt previously drawn may be restructured to meet Council risk or cost objectives.

8.3. The contribution the treasury management function makes to the authority is critical, as the balance of debt and investment operations ensure liquidity or the ability to meet spending commitments as they fall due, either on day-to-day revenue or for larger capital projects. The treasury operations will see a balance of the interest costs of debt and the investment income arising from cash deposits affecting the available budget. Since cash balances generally result from reserves and balances, it is paramount to ensure adequate security of the sums invested, as a loss of principal will in effect result in a loss to the General Fund Balance.

8.4. Whilst any commercial initiatives or loans to third parties will impact on the treasury function, these activities are generally classed as non-treasury activities, (arising usually from capital expenditure), and are separate from the day to day treasury management activities. These will be considered under the forthcoming *Investment Regeneration Strategy*.

8.5. CIPFA defines treasury management as:

"The management of the local authority's borrowing, investments and 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."

8.6. Revised reporting is required for the 2020/21 reporting cycle due to revisions of the MHCLG *Investment Guidance*, the MHCLG *Minimum Revenue Provision (MRP) Guidance,* the CIPFA *Prudential Code* and the CIPFA *Treasury Management Code*.

9. Treasury Management reporting

9.1. The Council is currently required to receive and approve, as a minimum, three main treasury reports each year, which incorporate a variety of policies, estimates and actuals:

a. **Prudential and treasury indicators and treasury strategy** (within this report at Appendix D) - The first, and most important, report is forward looking and covers:
   - the capital plans (including prudential indicators);
   - a minimum revenue provision (MRP) policy (how residual capital expenditure is charged to revenue over time);
   - the treasury management strategy (how the investments and borrowings are to be organised), including treasury indicators; and
   - an investment strategy (the parameters on how investments are to be managed).

b. **A mid-year treasury management report** – This is primarily a progress report and will update members on the capital position, amending prudential indicators as necessary, and whether any policies require revision.

c. **An annual treasury report** – This is a backward looking review document and provides details of a selection of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy.

9.2. The above reports are required to be adequately scrutinised before being recommended to the Council. This role is undertaken by the Finance and Audit Scrutiny Committee.

9.3. In addition, the revised CIPFA Prudential and Treasury Management Codes required, for 2019/20, all local authorities to prepare a **Capital Strategy** report, which provides the following:

- a high-level long-term overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of services
- an overview of how the associated risk is managed
- the implications for future financial sustainability.

9.4. The aim of the Capital Strategy is to ensure that all elected members on full Council understand the overall long-term policy objectives and the resulting capital strategy requirements, governance procedures and risk appetite.

9.5. This capital strategy is reported separately from the Treasury Management Strategy Statement; non-treasury investments will be reported through the former. This ensures the separation of the core treasury function under Security, Liquidity and Yield principles, and the policy and commercialism investments usually driven by expenditure on an asset. The capital strategy will show:

- The corporate governance arrangements for these types of activities;
- Any service objectives relating to the investments;
- The expected income, costs and resulting contribution;
- The debt related to the activity and the associated interest costs;
- The payback period (MRP policy);
- For non-loan type investments, the cost against the current market value;
- The risks associated with each activity.

9.6. Where a physical asset is being bought, details of market research, advisers used, (and their monitoring), ongoing costs and investment requirements and any credit information will be disclosed, including the ability to sell the asset and realise the investment cash.

9.7. As reported in the February 2020 *2020/21 General Fund Budget and Council Tax* report, the Capital Strategy that was approved for 2019/20 will be updated during 2020/21 to reflect significant new policies and strategies, including the Climate Emergency Declaration, the *Asset Management Strategy* and a pending *Investment Regeneration Strategy*.

9.8. Where the Council has borrowed to fund any non-treasury investment, there should also be an explanation of why borrowing was required and why the MHCLG Investment Guidance and CIPFA Prudential Code have not been adhered to.

9.9. Non-treasury investments that are for Investment Regeneration purposes will be subject to the new *Investment Regeneration Strategy*.

9.10. If any non-treasury investment sustains a loss during the final accounts and audit process, the strategy and revenue implications will be reported through the same procedure as the capital strategy, i.e. through the budget monitoring process and reports to members.

9.11. To demonstrate the proportionality between the treasury operations and the non-treasury operation, high-level comparators are shown throughout this report, where appropriate.