NOTTINGHAMSHIRE
Fire & Rescue Service
Creating Safer Communities

Nottinghamshire and City of Nottingham
Fire and Rescue Authority

TREASURY MANAGEMENT ANNUAL REPORT 2012/13

Report of the Treasurer to the Fire Authority

Agenda Item No:

Date: 27 September 2013

Purpose of Report:

To provide Members with an update on treasury management activity during the 2012/13 financial year.

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1. BACKGROUND

1.1 Treasury management is defined as:

"The management of the local authority's 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. "

1.2 The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management (revised in 2011) was adopted by the Fire Authority on 9 April 2010.

1.3 The primary requirements of the Code are as follows:

1. The creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Authority's treasury management activities.
2. The creation and maintenance of Treasury Management Practices which set out the manner in which the Authority will seek to achieve those policies and objectives.
3. Receipt by the Fire Authority of an annual Treasury Management Strategy Statement for the year ahead, a mid-year review report and an annual report covering activities during the previous year.
4. Delegation by the Authority of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.
5. Delegation by the Authority of the role of scrutiny of treasury management strategy and policies to a specific named body. For this Authority the delegated body is the Finance and Resources Committee.

1.4 This annual report has been prepared in compliance with CIPFA's Code of Practice, and covers the following:

- An economic review of 2012/13
- A review of Capital Activity during 2012/13 and the impact of this on the Authority's Capital Financing Requirement
- A review of the Investment and Cash Management Strategy during 2012/13.
- Investment and Cash Activity during 2012/13.
- A review of the Year End Investments and Cash Position and Usable Reserves
- A review of the Borrowing Strategy and Borrowing Activity during 2012/13
- A summary of compliance with Treasury and Prudential Limits for 2012/13

1.5 The Authority has appointed Sector Treasury Services as its external treasury management adviser.

2. REPORT

ECONOMIC REVIEW

2.1 The financial year 2012/13 continued the challenging investment environment of previous years i.e. low investment returns and continued heightened levels of counterparty risk. It had been expected that the Bank rate would rise towards the end of 2014 but this now seems unlikely due to a disappointing year in terms of economic growth. The Government maintained its tight fiscal stance but in February 2013 the credit rating agency Moody's downgraded the UK's AAA credit rating to AA+. The other two agencies have not followed suit as yet, but bringing the national debt down to a sustainable level within a reasonable time frame will be a key objective for the Government.

2.2 The Monetary Policy Committee increased quantitative easing by £50bn in July, because economic growth had been weak. This contributed to PWLB interest rates being at historically low levels. The EU sovereign debt crisis continued in the year, with both Greece and Cyprus receiving bailouts.

2.3 The Funding for Lending scheme announced in July resulted in cheap credit being made available to banks and, as a result, money market investment rates fell sharply in the second half of the year. However the announcement by the European Central Bank that it would do "whatever it takes" to support struggling Eurozone countries improved investor confidence in counterparties and there has been some evidence of a move away from only very short term investing.

REVIEW OF CAPITAL ACTIVITY IN 2012/13

2.4 The Authority undertakes capital expenditure on long term assets. These activities may either be:

- Financed immediately by way of capital or revenue resources (capital receipts, capital grants, revenue contributions), which does not give rise to a requirement to borrow; or

- If insufficient financing is available, or if a decision is taken not to apply resources, the capital expenditure will need to be financed by borrowing.

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

	2011/12 Actual	2012/13 Estimate	2012/13 Actual
	£000's	£000's	£000's
Capital Expenditure	2,879	5,573	2,430
Resourced By:			
- Capital Grants	1,486		1,616
- Capital Receipts	25		
- Revenue Contributions	1,368		814
- Internally Financed up to level of MRP	0		0
- Borrowing	0		0
Total Financed Capital Expenditure	2,879	5,573	2,430

2.6 Actual capital expenditure was within the prudential indicator set of £5,573k. At 31 March 2013, the Authority's capital financing requirement was £25,004k, which exceeded the prudential indicator set of £24,922k, due to actual factors affecting the capital financing requirement being different from assumptions used at the time the indicator was set. The amount by which the indicator was exceeded was £82k, which is a relatively small amount and this difference does not present a risk to the Authority. The Capital Financing Requirement (CFR) figure represents the Authority's underlying need to borrow to fund capital expenditure and equates to un-financed capital expenditure which has not yet been paid for by revenue funding or other resources such as capital grants or receipts. The CFR is reduced over time by way of a statutory Minimum Revenue Provision charge to revenue which effectively charges the revenue budget for the use of capital assets over their asset lives.

REVIEW OF THE INVESTMENT AND CASH MANAGEMENT STRATEGY

2.7 The Treasury Management Strategy approved by the Authority set out the policies for managing investments and for giving priority to the security and liquidity of those investments. The risk appetite of this Authority is low in order to give priority to security of its investments. Accordingly the following types of low risk specified investments may be made:

- Deposits with the Debt Management Agency (Government)
- Term deposits with Banks and Building Societies
- Term Deposits with uncapped English and Welsh local authority bodies
- Triple-A rated Money Market Funds
- UK Treasury Bills

During the year, all investments were made with banks, building societies and other local authority bodies.

2.8 The Authority will aim to limit its investment with any single counterparty to £2m although the strategy noted that this was sometimes difficult to achieve. No term deposits will be made for more than 1 year without the prior approval of the Treasurer and the Chair of Finance and Resources Committee. The selection of counterparties with a high level of creditworthiness will be achieved by reference to Sector's weekly credit list of potential counterparties. The Sector weekly credit list shows potential investment counterparties, which are colour-coded to indicate the maximum period it is recommended that investments are made for. The Authority will therefore use counterparties with the following durational colour codes:

- Blue - investments up to 1 year (only applies to nationalised or semi nationalised UK Banks)
- Orange – investments up to 1 year
- Red – investments up to 6 months
- Green - investments up to 3 months

The Authority has made all investments with counterparties during the year in accordance with the maximum periods advised by Sector.

2.9 The Authority will avoid locking into longer term deals while investment rates are down at historically low levels unless exceptionally attractive rates are available which make longer term deals worthwhile.

2.10 In terms of cash resources, the strategy is to maintain a bank overdraft facility of £200,000, to continue to use cash flow forecasting to predict cash surpluses and shortfalls so that these can be managed and to invest small bank account balances in the Business Premium Account on a daily basis.

2.11 All aspects of the treasury management strategy outlined for 2012/13 remained in place throughout the year. The Strategy included a forecast for the bank rate, which showed that this was expected to be at 0.5% by 31 March 2013. The bank rate has remained at 0.5% throughout the year and beyond.

INVESTMENT AND CASH ACTIVITY IN 2012/13

2.12 As at 31 March 2013, the Authority held £12.128m of principal as short term investments. This comprised 9 separate investments with 9 counterparties, none of which was more than £2m. Two of the investments were with Local Authorities, five were with banks, one was held with a building society and one with the NFRS trading company. At the time of writing this report, seven of these investments had matured and been repaid.

2.13 During the course of the year, 20 investments were made, excluding the overnight sweep to the Business Premium Account. None of these exceeded £2m in value. The longest term investment placed was for 364 days and all investments were made in accordance with the Authority's credit rating criteria policy. There were occasions when the amount invested with the Authority's own bank (Barclays Bank) exceeded £2m due to difficulties at those times in placing funds with counterparties meeting our credit rating criteria.

2.14 The 3 Month LIBID benchmark rate for the year was 0.567%. The Authority's investments earned an average rate of 0.747% during the year resulting in total investment income earned of £143k. This was in excess of the budgeted sum for investment income of £50k and was mainly due to surplus cash being higher than expected as a result of the revenue budget underspend and cash backed reserves being invested.

2.15 Nottinghamshire Fire and Rescue Service (Trading) Limited was set up as a subsidiary company during 2010/11. A bank account for the company was opened with Barclays Bank, who required funding to be paid into the account to cover possible working capital shortfalls. To accommodate this, a loan of £54,999 was made to NFRS (T) Ltd in the form of a revolving credit facility which can be repaid at any time with one week's notice by either party. An arms-length variable interest rate was agreed at 15 basis points above the Bank of England bank rate. The loan is shown as a short term investment in the Authority's accounts and as a loan in the trading company's accounts. During 2012/13 a further £10,000 of the loan was repaid to the Authority, leaving an outstanding balance of £39,999.

2.16 During the year, the Authority's overdraft facility was not used.

REVIEW OF INVESTMENTS / CASH POSITION AND USABLE RESERVES

2.17 Members will be aware that the Authority's "usable" reserves i.e. the General Fund and Earmarked Reserves have not been fully cash backed in the past due to the internal financing of capital expenditure in previous years. This was a particular issue during the "credit crunch" period in 2008 when Members approved an interim treasury strategy to delay borrowing, thereby avoiding an increase in cash balances whilst the money markets were suffering a degree of turmoil and credit ratings were volatile.

2.18 Since then the position has improved: at 31 March 2013, the value of the Authority's usable reserves totalled £12,328k. The balance sheet as at the same date shows that short term investments were valued at £12,128k and cash held totalled £864k. Members can therefore be assured that if the Authority needs to spend some of its usable reserves, there is sufficient liquidity in its financial position to be able to do so.

REVIEW OF THE BORROWING STRATEGY AND BORROWING ACTIVITY IN 2012/13

2.19 The strategy recommended that capital grant and a capital receipt from the sale of Dunkirk Fire Station would be used to finance capital expenditure during 2012/13. A capital grant of £1,486k was applied to finance expenditure but due to the delay in the sale of Dunkirk Fire Station and a revenue budget underspend, further funding was obtained by way of direct revenue contributions, which had been budgeted.

2.20 No borrowing was undertaken during 2012/13 as £3,000k of borrowing was undertaken in September 2010 for the financing of the capital programme in 2010/11, 2011/12 and 2012/13. Subsequently on 1 April 2011, Members of the Finance & Resources Committee accepted a proposal to bring forward revenue financing of the capital programme for 2010/11 and 2011/12. This meant that £2,000k of the £3,000k loan was not used to finance the capital programme. In September 2013, a PWLB loan will be repaid and this surplus borrowing will be used to partially fund the repayment.

2.22 The treasury management limits to loan maturity were set in 2012/13 and are shown below :

Loan Maturity		
	Upper Limit	***Lower Limit***
Under 12 months	20%	0%
12 months to 5 years	30%	0%
5 years to 10 years	75%	0%
10 years to 20 years	100%	0%
Over 20 years	100%	30%

Members can be reassured by the fact that 35% of outstanding debt will mature in more than 20 years' time and the loan of £3m, which matures in 2013/14 will only need to be replaced by a £1m new loan and PWLB rates remain low.

2.23 No rescheduling of debt has taken place to date, as the interest rate climate has not resulted in an advantageous environment for rescheduling.

2.24 The Authorised Limit is the affordable borrowing limit above which the Authority does not have the power to borrow. This was set at £31,641k for 2012/13. Total borrowing as at 31 March 2013 was £25,540k, which was well within the Authorised limit.

2.25 The Operational Boundary is the expected borrowing position of the Authority within the year. This was set at £28,764k for 2012/13, and was not exceeded at any point during the year.

SUMMARY OF COMPLIANCE WITH TREASURY AND PRUDENTIAL LIMITS

2.27 The following indicators were approved by Members for the 2012/13 financial year. Actual performance is shown in the final column of the table below.

2.28 The indicator for the Incremental Impact of New Capital Investment Decisions on Council Tax shows an actual result of £2.19 compared to an estimate of £1.96. The reason for this difference is mainly due to the fact that the 2011/12 capital financing costs were lower than had been estimated which resulted in a higher incremental change.

Treasury or Prudential Indicator or Limit	Approved for 2012/13	Actual for 2012/13
Estimate of Ratio of Financing Costs to Net Revenue Stream	7.7%	7.8%
Estimate of the Incremental Impact of New Capital Investment Decisions on the Council Tax (Band D)	£1.96	£2.19
Estimate of Total Capital Expenditure to be Incurred	£5,573,000	£2,430,000
Estimate of Capital Financing Requirement	£24,922,000	£25,004,000
Operational Boundary	£28,764,000	Not exceeded
Authorised Limit	£31,641,000	Not exceeded
Upper limit for fixed rate interest exposures	100%	100%
Upper limit for variable rate interest exposures	30%	0%
Loan Maturity:	Limits:	Limits:
Under 12 months	Upper 20% Lower 0%	12%
12 months to 5 years	Upper 30% Lower 0%	25%
5 years to 10 years	Upper 75% Lower 0%	17%
10 years to 20 years	Upper 100% Lower 0%	11%
Over 20 years	Upper 100% Lower 30%	35%
Upper Limit for Principal Sums Invested for Periods Longer than 364 Days	£2,000,000	Not applicable

3. FINANCIAL IMPLICATIONS

The financial implications of this report are set out in full within the body of the report.

4. HUMAN RESOURCES AND LEARNING AND DEVELOPMENT IMPLICATIONS

There are no human resources or learning and development implications arising directly from this report.

5. EQUALITIES IMPLICATIONS

An equality impact assessment has not been done because this report gives a review of activities rather than introducing a new policy.

6. CRIME AND DISORDER IMPLICATIONS

There are no crime and disorder implications arising directly from this report.

7. LEGAL IMPLICATIONS

There are no legal implications arising directly from this report, other than the requirement to act within the Authority's powers when undertaking treasury management borrowings and investments.

8. RISK MANAGEMENT IMPLICATIONS

Risk management is a key aspect of treasury management, and the Treasury Management Strategy sets out the parameters within which activities will be carried out with a view to managing credit risk, liquidity risk, re-financing risk and market risk. The Authority has approved a prudent approach to treasury management and this report allows Members to review how well risks have been managed during the year.

9. RECOMMENDATIONS

It is recommended that Members note the contents of this report.

10. BACKGROUND PAPERS FOR INSPECTION (OTHER THAN PUBLISHED DOCUMENTS)

None.

Peter Hurford
TREASURER TO THE FIRE AUTHORITY