APPENDIX 1

EXECUTIVE BOARD - 22 FEBRUARY 2011

Title of paper:	**TREASURY MANAGEMENT 2011/12 STRATEGY**	
Director(s)/ Corporate Director(s):	Carole Mills-Evans Deputy Chief Executive & Corporate Director for Resources	**Wards affected:** All
Portfolio Holder(s):	Councillor Graham Chapman, Deputy Leader and Portfolio Holder for Resources, Economic Development and Reputation	**Date of consultation with Portfolio Holder(s):** 19 January 2011
Contact(s) and contact details:	Jeff Abbott, Head of Corporate and Strategic Finance (0115 8763648 * jeff.abbott@nottinghamcity.gov.uk	
Others who have provided input:	Pete Guest, Treasury Management Officer (0115 8764163 * pete.guest@nottinghamcity.gov.uk	

Key Decision:	No
Reasons for Key Decision:	
Expenditure of £500,000 or more in a single year	
Revenue income of £500,000 or more in a single year	
Savings of £500,000 or more in a single year	
Capital expenditure of £1,000,000 or more	
Capital income of £1,000,000 or more	
Significant effects on communities living or working in an area comprising two or more wards in the City	
Relevant Council Plan Strategic Priority:	
World Class Nottingham	✓
Work in Nottingham	✓
Safer Nottingham	✓
Neighbourhood Nottingham	✓
Family Nottingham	✓
Healthy Nottingham	✓
Serving Nottingham Better	✓

Summary of issues (including benefits to customers/service users):

This report sets out the treasury management and investment strategies for 2011/12 including the debt repayment strategy (**Annexe 1**). The associated Prudential Indicators are shown within an appendix to the strategy, along with existing risks and a glossary of technical terms.

Recommendation(s):

1 To endorse and recommend for approval by the City Council at its meeting on 7 March 2011:

- The overall Treasury Management Strategy for 2011/12 **(Annexe 1)**
- The strategy for debt repayment in 2011/12 **(section 5** of **Annexe 1)**
- The Investment Strategy for 2011/12 **(section 6** of **Annexe 1)**
- The prudential indicators and limits from 2009/10 to 2013/14 **(Appendix A** within **Annexe 1)**

1 BACKGROUND

1.1 Treasury management is a term used to describe the management of an organisation's borrowing and investments, their associated risks and the pursuit of optimum performance or return consistent with those risks.

1.2 The treasury management function is governed by provisions set out under Part 1 of the Local Government Act 2003, whereby the City Council must have regard to the CIPFA Prudential Code and the CIPFA Code of Practice.

1.3 The City Council retains external advisors to provide additional input on treasury management matters. The service provided includes economic and interest rate forecasting, advice on strategy, portfolio structure, debt restructuring, investment policy, creditworthiness, credit ratings and other counterparty criteria and technical assistance on other related matters, as required.

1.4 The Treasury Management and Investment Strategies will be considered by Audit Committee on 25 February 2010, as part of the scrutiny process required by the CIPFA Code. Any decisions of that Committee will be reflected in the report submitted to City Council for final approval.

2 REASONS FOR RECOMMENDATIONS (INCL. OUTCOMES OF CONSULTATION)

2.1 To comply with:

- Financial Regulations and the CIPFA Code of Practice on Treasury Management by submitting a policy and strategy statement for the ensuing financial year.
- Guidance issued by the Secretary of State under section 15(1) (a) of the Local Government Act 2003 in approving, at Council, an Annual Investment Strategy before 1 April.
- Guidance issued by the Secretary of State under the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 which requires the preparation of an annual statement of the Council's policy on making a Minimum Revenue Provision (MRP).

3 TREASURY MANAGEMENT AND INVESTMENT STRATEGY 2011/12

3.1 This document sets the strategic context, within the Council's planning cycle, for how treasury management activity will take place. The various aspects of the strategy (i.e. treasury, investment and debt) are embraced within one overall document known as the Treasury Management Strategy which is set out at **Annexe 1**. Within this context, the objectives of the strategy are:

- To achieve the lowest net interest rate costs on the City Council's external debt, whilst recognising the risk management implications.
- To protect the Medium Term Financial Plan (MTFP) from the unbudgeted financial impact of fluctuations in interest rates and to prevent the need for excessive borrowing in future years when rates may be unfavourable.
- To maintain the security and liquidity of external investments, and within those parameters, to seek to maximise the return on such investments.

3.2 Department for Communities for Local Government (DCLG) guidance on local authority investments requires an annual investment strategy to be in place before the financial year in which it applies. This document is incorporated within the Treasury Management Strategy and provides details of the ways in which investments will be managed to protect the Council's financial position and the value of funds invested, whilst ensuring that the returns obtained are appropriate given the stated attitude to risk. The DCLG guidance reiterates security and liquidity as the primary objectives of a prudent investment policy.

3.3 The 2011/12 strategy document reflects recommendations made by Audit Committee in respect of the 2010/11 strategy, as part of its scrutiny role:

- The inclusion of the Treasury Management Risk Management Action Plan within the strategy document
- More detail of the means by which the cost of debt would be managed
- A summary of the current investment strategy and
- The reasoning behind the differing investment limits for UK and overseas banks

The main changes to the proposed strategy for 2011/12 are in respect of the eligible counterparties for investment:

- The extension of the maximum duration for UK deposits to 2 years
- The inclusion of a number of additional non-UK banks for term deposits
- The deletion of Spanish banks from the non-UK list for term deposits
- The addition of Supranational Bonds to the counterparty list.

4 PRUDENTIAL INDICATORS (ANNEXE 1, APPENDIX A)

4.1 The Prudential Code
The Code requires a series of Prudential Indicators (PIs) to be set and approved for the forthcoming and following two financial years. These financial indicators are derived from proposed treasury management activity and provide insight into the financial impact of activities. **Appendix A** within the Treasury Management Strategy at Annexe 1 sets out the indicators for 2011/12 to 2013/14 that are expected to be generated by the proposed strategies, along with explanatory notes.

4.2 Nottingham Express Transit Phase 2
The proposed financing of the construction of lines 2 and 3 of the existing tram system (NET Phase 2) and the transfer of the existing tram system to the successful bidder includes significant prudential borrowing by the City Council, with the first tranche of borrowing currently scheduled for 2011/12. At this stage, the PIs in this report make no provision for this debt, the level of which remains to be determined.

Executive Board approval for the final NET Phase 2 scheme will be required before financial close. When that report is submitted, City Council approval will also be sought for the appropriate amendments to the PIs.

5 OTHER OPTIONS CONSIDERED IN MAKING RECOMMENDATIONS

5.1 Options for management of the City Council's debt and investment portfolio are continually reviewed. The overall aim is to minimise the net revenue costs of the debt whilst maintaining an even debt profile in future years, and to maximise investment returns within stated security and liquidity guidelines.

6 FINANCIAL IMPLICATIONS (INCLUDING VALUE FOR MONEY)

6.1 Total treasury management payments comprise interest charges and receipts and provision for repayment of debt. A proportion of the City Council's debt relates to capital expenditure on council housing and this is recharged to the Housing Revenue Account (HRA) and funded through the Housing Subsidy system. The remaining costs are included within the treasury management section of the General Fund budget. **Table 1** sets out the budget for 2011/12:

TABLE 1: REVENUE BUDGET POSITION			
DESCRIPTION	**BUDGET 2010/11 £m**	**FORECAST OUTTURN 2010/11 £m**	**BUDGET 2011/12 £m**
External interest	27.634	22.931	23.703
Debt repayment provision	13.940	13.244	16.631
Less: HRA recharge	(14.224)	(11.403)	(11.629)
General Fund expenditure	**27.350**	**24.772**	**28.705**
Investment interest	(2.157)	(1.376)	(1.885)
Prudential borrowing recharge	(1.607)	(1.600)	(1.303)
Treasury Management Reserve	-	1.865	3.310
NET GENERAL FUND POSITION	**23.586**	**23.661**	**28.827**

The 2010/11 forecast outturn is £1.865m less than the original budget. This saving has arisen through the active management of the debt and investment portfolios. At this stage, this sum has been transferred into the Treasury Management Reserve.

The 2011/12 budget of £28.827m is included in the MTFP for 2011/12 – 2013/14, included elsewhere on the agenda for this meeting. Included within this figure is an annual repayment cost of £2.844m for the equal pay capitalisation of £10.5m in 2010/11.

A forecast reduction in the 2011/12 borrowing requirement, together with management of the debt and investment portfolios provide an estimated £3.310m of savings in 2011/12. However, in light of current economic and financial uncertainties, this sum has been retained within the Treasury Management Reserve.

7 RISK MANAGEMENT ISSUES (INCLUDING LEGAL IMPLICATIONS, CRIME AND DISORDER ACT IMPLICATIONS AND EQUALITY AND DIVERSITY IMPLICATIONS)

7.1 Risk management plays a fundamental role in treasury activities, due to the value and nature of transactions involved. The management of specific treasury management risks is set out in the Manual of Treasury Management Practices and Procedures and a risk register is prepared for the treasury function.

The key Strategic Risk relating to treasury management is SR17 'Failure to protect the Council's investments'. The current rating for this risk is 6 (Likelihood = unlikely, Impact = moderate) which represents a reduction from the previous rating. Details of the Risk Management Action Plan are provided in Annexe 1 Appendix B.

8 EQUALITY IMPACT ASSESSMENT

8.1 This report does not contain proposals for new or changing services or functions.

9 LIST OF BACKGROUND PAPERS OTHER THAN PUBLISHED WORKS OR THOSE DISCLOSING CONFIDENTIAL OR EXEMPT INFORMATION

9.1 PWLB records, working papers

10 PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

10.1 Local Authorities (Capital Finance and Accounting) regulations 2008
The Prudential Code for Capital Finance in Local Authorities 2009 – CIPFA
Treasury Management in the Public Services, Code of Practice 2009 – CIPFA

NOTTINGHAM CITY COUNCIL

TREASURY MANAGEMENT STRATEGY 2011/12

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Executive Board 22 February 2011
City Council 7 March 2011

TREASURY MANAGEMENT AND INVESTMENT STRATEGY 2011/12

1. Context

Medium Term Financial Strategy (MTFS)
The MTFS sets out the arrangements for the planning and management of the Council's finances. Section G sets out the overall context for the Council's treasury management activities. The three strategic principles set out there are as follows:

G1	All borrowing and debt management activity will be carried out in accordance with the annually approved Treasury Management Strategy and the Manual of Treasury Management Practices and Procedures, and within approved Prudential Indicators, having the highest regard for prudence, affordability and sustainability in the longer term.
G2	The management of the treasury investment portfolio will be in accordance with the approved investment strategy, with all investments complying with counterparty limits and restrictions.
G3	Appropriate use of prudential borrowing to fund capital investment will be made within prudential indicators and subject to medium term affordability.

The Debt Portfolio
Management of the City Council's debt portfolio is a key element of the Treasury Management and Investment Strategy. At 31 March 2011 the total value of the portfolio is c £515m (excluding PFI 'debt'), borrowed at an average interest rate of 4.40%. In 2011/12 total debt is forecast to increase to c £541m (again, excluding PFI-related debt.) Gross interest on all debt in 2011/12 is estimated at c £23.844m.

The Investment Portfolio
The City Council also maintains an investment portfolio to ensure that surplus cash (i.e.: working capital, reserves and provisions) earns interest whilst it is being held. The average value of investments during 2010/11 is estimated at c £118m. In 2011/12 an average balance of c £110m is forecast.

The average return on investments during 2010/11 is expected to be 1.04%. With short-term interest rates expected to increase gradually during 2011/12, the average return on investments is forecast to rise to 1.60% for the year.

Market Conditions
The Treasury Management Strategy seeks to protect the City Council from market related risks by proactively monitoring key factors such as interest rates and economic opinions, both nationally and internationally. The adopted strategy will be regularly reappraised and, if necessary, realigned to reflect market conditions and changes to interest rate forecasts.

Outlook for interest rates
The Bank of England base rate has remained at its all-time low of 0.50% since March 2009. The current forecast is for this rate to begin to rise in late 2011, reaching 1.25% by the end of the financial year. Longer-term rates are expected to rise throughout 2011/12.

Table 1 shows actual interest rates at 31 December 2010 and projected rates until the end of March 2013, based on forecasts from the City Council's advisors. Short-term rates inform decisions on the investment of surplus monies, and rates for long-term borrowing are linked to the Government Gilt rates for the appropriate period.

TABLE 1: PROJECTED MOVEMENTS IN INTEREST RATES 2010 - 2013								
YEAR	**END PERIOD**	**BASE RATE**	**MONEY RATES**			**LONG TERM GILT RATES**		
			3 MONTHS	**6 MONTHS**	**12 MONTHS**	**5 YEARS**	**20 YEARS**	**50 YEARS**
2010	Dec	0.50	0.70	1.00	1.50	2.00	4.25	4.25
2011	Mar	0.50	0.70	1.00	1.75	2.25	4.50	4.25
	Jun	0.50	0.95	1.25	2.00	2.75	4.75	4.50
	Sep	0.75	1.20	1.50	2.25	3.25	5.00	4.75
	Dec	1.00	1.45	1.75	2.50	3.50	5.00	4.75
2012	Mar	1.25	1.70	2.00	2.75	3.75	5.00	4.75
	Jun	1.50	2.00	2.50	3.00	4.00	5.00	4.75
	Sep	2.00	2.70	3.00	3.25	4.00	5.00	4.50
	Dec	2.50	2.95	3.25	3.50	4.00	5.00	4.50
2013	Mar	2.75	2.95	3.25	3.50	4.00	5.00	4.50

Interest rate forecasts are usually prepared with an 'upside' and a 'downside' risk, because they may move more or less than forecast. The current conflict is between preventing the economy returning to recession (keeping a low base interest rate for longer) and a desire to curb inflationary pressures (increasing base rates faster). Following the recent Gross Domestic Product figures for the last quarter of 2010, the stronger risk may be that short-term rates will rise slower than the above forecasts.

2. Strategic Principles

The Council's treasury management activities will be undertaken with the following strategic aims and objectives:

1. To achieve the minimum interest rate cost on the City Council's external debt, whilst recognising the risk management implications;
2. To protect the capital value of external cash investments and ensure the liquidity of those investments;
3. To provide an income stream to the City Council from investments and maximise this stream, within the stated parameters of security and liquidity;
4. To apply mitigation to the risks associated with treasury management activity;
5. To seek to follow best practice at all times.

The actual outcomes against these strategic principles can be assessed by the use of prudential indicators and associated commentary. **Table 2** lists which of the prudential indicators set out in **Appendix A** relate to each of the principles.

TABLE 2: STRATEGIC PRINCIPLES LINK TO PRUDENTIAL INDICATORS	
PRINCIPLE	**PIs**
1	2i, 2iii, 2iv, 3i, 3ii, 3iii, 3v
2	3iv, 3v
3	3iv, 3v
4	3v
5	3v

Within these principles, specific strategies will be adopted in 2011/12 in respect of:

- Borrowing
- Debt rescheduling
- Provision for repayment of debt
- Investments
- Reporting, and
- Training

These strategies are addressed in the following paragraphs.

3. Borrowing Requirement and Strategy

The City Council undertakes borrowing to:

- Finance capital expenditure not met from other sources (e.g. grants, capital receipts etc.)
- Replace maturing debt (net of minimum revenue provision)
- Finance cash flow in the short-term

The primary risks associated with the management of a debt portfolio are the uncertain future fluctuations in interest rates and an uneven loan maturity profile, requiring large amounts of debt to be replaced in any single period. To mitigate this risk, the City Council's debt portfolio will be managed with the aim of reducing the annual revenue cost of borrowing and evenly spreading the debt maturity profile. **Table 3** shows the estimated total borrowing requirement for 2011/12, reflecting the current capital programme:

TABLE 3: TOTAL BORROWING REQUIREMENT 2011/12	
	£m
Debt maturing during the year	12.000
Supported borrowing 2011/12:	
HRA	-
General Fund	-
Unsupported borrowing 2011/12:	
HRA	-
General Fund	24.967
Less: revenue provision for repayment:	
HRA	(0.702)
General Fund	(16.942)
TOTAL	**19.323**

The City Council can raise borrowing from the following sources:

- The Public Works Loan Board (PWLB)
- Other local authorities
- Money markets
- Direct from commercial banks and other institutions
- Local authority stock issues
- Local authority Bills
- Structured finance

As part of the Comprehensive Spending Review announced by central Government in October 2010, PWLB rates were increased to 1% above the cost of the Government's own borrowing, to control public sector debt. Nevertheless, the PWLB still remains an attractive source of borrowing. The type, period, and timing of new borrowing will be determined by the Chief Finance Officer (CFO), under delegated authority, taking into account the following factors:

- Expected movements in interest rates
- The maturity profile of existing debt
- The impact on the medium term financial strategy
- Prudential indicators and limits

The use of variable rate borrowing will be continued whilst interest rates remain favourable. In 2010/11, with the average return on investments at around 1%, and the cost of long-term borrowing being >4%, surplus cash was used to replace long-term borrowing on a temporary basis. With this differential between short-term investing and long-term borrowing forecast to continue in 2011/12, it is expected that internal resources, used in lieu of borrowing, will again be a cost-effective means of financing capital expenditure in 2011/12.

4. Debt Restructuring

Opportunities for debt restructuring, which involves the premature replacement of existing debt with new loans for different periods and at different rates, will be monitored and appropriate action taken by the CFO under delegated authority, taking into account the following factors:

- The maturity profile
- Ongoing revenue savings
- The impact of premiums and discounts
- The impact on Prudential Indicators

In particular, existing Public Works Loan Board (PWLB) variable rate debt and market loans with lender options will be monitored against prevailing interest rates. Where it is considered beneficial to do so, restructuring into fixed-rate products may be undertaken, to reduce the risk of future interest rate movements.

5. 2011/12 Minimum Revenue Provision (MRP) Statement

Under the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 (S.I. 2008/414), local authorities have a duty to produce an annual statement on their policy for making a minimum revenue provision (MRP) for the repayment of outstanding debt. For 2011/12 the City Council will adopt the following policies in determining the MRP:

- For capital expenditure financed through borrowing prior to 31 March 2008, the regulatory method (designated by the Regulations as Option 1) will be adopted – i.e.: the MRP will be 4% of the opening capital financing requirement (CFR).
- For capital expenditure incurred after 1 April 2008, and financed by supported borrowing, the regulatory method will be adopted (Option 1).
- For capital expenditure incurred after 1 April 2008, and financed by unsupported borrowing (General Fund and HRA), the authority will adopt the asset life method

(Option 3). The MRP will be based on the capital expenditure divided by a determined asset life to give equal annual instalments. Once the asset life has been determined for this capital expenditure, it will not be altered in future years, for MRP repayment purposes.

The 2010 Code of Practice on Local Authority Accounting (based on IFRS) requires local authorities to adopt International Financial Reporting Standards, from 1 April 2010. In 2009/10, the 2009 SORP required some of the City Council's existing PFI schemes or leases being brought onto the balance sheet in preparation for the move to IFRS. Where this has occurred, there has been an increase in the City Council's overall CFR (its need to borrow) and, therefore, an increase in the MRP charge to revenue. MRP for these items matches the annual principal repayment for the associated deferred liability. The effect on the City Council's revenue account is therefore neutral.

6. Investment Strategy 2011/12

<u>Investment Policy</u>
All external investments will be made in accordance with the City Council's adopted investment policy and prevailing legislation and regulation. In accordance with CLG guidance, the City Council's general policy objective is to invest its surplus funds prudently. The investment priorities are:

- Security of the invested capital
- Liquidity of the invested capital
- And, commensurate with security and liquidity, an optimum return on investments

During 2010/11, investments with UK banks and building societies were restricted to those institutions that had access to the Government's Credit Guarantee Scheme, set up to provide a platform to maintain the solvency of institutions critical to the UK's financial stability. In addition, a number of non-UK institutions were included on the list of approved counterparties, based on a range of criteria. A maximum period of 264 days was applied to all investments, with some counterparties being limited to shorter periods.

Actual investments to date in 2010/11 have been limited to instant access call accounts and period deposits with UK banks and Money Market Funds. As a consequence of the base interest rate remaining at 0.50% throughout the period, the average return to 31 December 2010 was 1.01%, against an original budget estimate of 1.40%.

For 2011/12, the following changes are recommended:

- The extension of the maximum duration for UK deposits to 2 years
- The inclusion of Svenska Handelsbanken (Sweden) for non-UK bank term deposits
- The deletion of Spanish banks from the non-UK list for term deposits
- The addition of Supranational Bonds

<u>Specific investment criteria</u>
The selection of counterparties eligible for investment in 2011/12 has been based on advice received from our advisors and has taken into account all appropriate credit ratings of those institutions (using the lowest available rating from those supplied by the three main rating agencies). In addition, a range of other factors have been taken into account, including:

- The existence of Government support schemes or statements of potential government support
- Individual counterparty and Government credit ratings
- Credit default swap rates (where quoted)
- Share prices (where quoted)
- Press articles and reports
- Any other information pertinent to the security of the investment

All investments are required to be categorised as ‘Specified’ or Non-Specified’, based on criteria in the CLG guidance. To qualify as a Specified Investment, the investment is required to be:

- In sterling only
- For a maximum period of 364 days
- With a counterparty of a high credit quality, as determined by the City Council
- Not defined as capital expenditure under section 25(1)(d) in SI 2003 No 3146

Any investments not meeting the above requirements are deemed to be Non-Specified investments.

The categories of investment identified for use within the above criteria in 2011/12 are:

- Deposits with the Government’s Debt Management Account Deposit Facility
- Deposits with other UK local authorities
- Deposits with UK banks and building societies meeting the high credit quality, as determined by the City Council and included on the City Council’s approved counterparty list
- Deposits with non-UK banks included on the City Council’s approved counterparty list
- Money Market Funds (pooled, short maturity, high quality investment vehicles offering instant access) with a AAA rating and a Constant Net Asset Value
- AAA-rated Supranational Bonds (the debt of international organizations such as the World Bank, the Council of Europe and the European Investment Bank)
-

<u>Approved investment counterparty list</u>
The proposed counterparty list, shown in **Table 4**, has been drawn up after evaluating and applying the above criteria for available institutions. For all banks, a minimum long- and short-term credit rating from all three rating agencies (Fitch, S&P and Moodys) has been applied as follows:

- a short-term rating of F1 (Fitch), A-1 (S&P) or P-1 (Moodys)
- and a long-term rating of A+ (Fitch and S&P) or A1 (Moodys)

The interpretation of these various credit ratings is provided as a note to **Table 4.** Regular monitoring and evaluation of credit ratings and other criteria will be maintained, and counterparties will be removed from the approved list if this combined evaluation falls below the minimum level. This action will also be taken if other intelligence suggests that this would be prudent.

Limits on periods of investment and maximum sums to be deposited have been applied to individual institutions, based on the evaluation of the above criteria and strengthened through reference to the size of the investment portfolio, the remaining period of Government guarantees, banking group structures and country limits. The higher limits for UK institutions reflects their inclusion within the Government Credit Guarantee Scheme – an indication of their deemed systemic importance within the UK banking system.

The details of all limits applied are provided in **Table 4** and the associated notes - in particular:

- Co-Operative Bank – the City Council's own bank, while not meeting the minimum criteria for investments, is included on the counterparty list for periods of up to 5 days, to accommodate necessary short-term cash management.
- Group limits – where more than one bank on the counterparty list is included within a banking group (e.g. Bank of Scotland and Lloyds TSB Bank), individual limits will also apply to the group as a whole.
- Country limits – other than for UK institutions, a total investment limit will apply to all counterparties in a particular country. No more than 10% of the total investment portfolio, at the time of the deposit, will be placed with any one country.
- Overall country limit – in addition, no more than 25% of the investment portfolio, at the time of the deposit, will be placed with non-UK banks in total.
- Supranational Bonds e.g. European Investment Bank/Council of Europe – a maximum sum of £20m.
- Money Market Funds – as well as individual limits, a maximum sum of £40m will be held in MMFs in total, at any one time.

TABLE 4: ELIGIBLE COUNTERPARTIES FOR INVESTMENT 2011/12

INSTRUMENT	COUNTRY	COUNTERPARTY	MAX. SUM	MAX. PERIOD
Term deposit / Call account	U.K.	Debt Management Office	No limit	No limit
		UK local authorities	No limit	2 years
		Bank of Scotland / Lloyds TSB Bank	£20m	2 years
		Barclays Bank	£20m	2 years
		Co-Operative Bank	No limit	5 days
		Clydesdale Bank	£20m	2 years
		HSBC Bank	£20m	2 years
		Nationwide Building Society	£20m	2 years
		Royal Bank of Scotland / Nat West Bank / Standard Chartered	£20m	2 years
		Santander UK (Abbey National)	£20m	2 years
	Australia	Australia & NZ Banking Group	£5m	364 days
		Commonwealth Bank of Australia	£5m	364 days
		National Australia Bank Ltd	£5m	364 days
		Westpac Banking Corporation	£5m	364 days
	Canada	Bank of Montreal	£5m	364 days
		Bank of Nova Scotia	£5m	364 days
		Canadian Imp. Bank of Commerce	£5m	364 days
		Royal Bank of Canada	£5m	364 days
		Toronto-Dominion Bank	£5m	364 days
	Finland	Nordea Bank Finland	£5m	364 days
	France	BNP Paribas	£5m	364 days
		Calyon	£5m	364 days
		Credit Agricole SA	£5m	364 days
		Soc Gen	£5m	364 days

	Germany	Deutsche Bank AG	£5m	364 days
	Netherlands	Rabobank	£5m	364 days
		ING Bank	£5m	364 days
	Sweden	Svenska Handelsbanken	£5m	364 days
	Switzerland	Credit Suisse	£5m	364 days
	USA	JP Morgan	£5m	364 days
Supranational Bonds	World-wide	E.g. European Investment Bank/Council of Europe/World Bank	£20m	2 years
Money Market Funds	World-wide	AAA-rated funds (Constant Net Asset Value)	£10m / fund	N/A

IMPORTANT NOTES TO TABLE 4:

<u>Credit Rating Definitions</u>

Short Term Ratings

Fitch F1
Highest credit quality, indicating the strongest capacity or timely payment of commitments.

Standard & Poor's A-1
Strong capacity to meet its financial commitments.

Moody's P-1
Offers superior credit quality and a very strong capacity for timely payment of short-term deposit obligations.

Long Term Ratings

Fitch A+
High credit quality. 'A' ratings denote expectations of low credit risk. They indicate strong capacity for payment of financial commitments. The '+' denotes the relative status within the category.

Standard & Poor's A+
An obligor rated 'A' has strong capacity to meet its financial commitments. The '+' denotes the relative status within the category.

Moody's A1
Banks rated A are considered upper-medium grade and are subject to low credit risk. The modifier 1 indicates that the rating is in the higher end of its generic rating category.

<u>Limiting Factors</u>

Co-operative Bank – *the City Council's own bank does not meet the City Council's applied criteria. They are included on the counterparty list, with a maximum period of investment of 5 days, for cash flow purposes.*

Groups *- where more than one institution is included within a banking group, the individual limit will apply to the total investment in that group*

Countries *- a maximum of 10% of the investment portfolio to be invested in any one country (excluding the UK) at the time of investment, with a maximum of 25% of the portfolio, at the time of investment, in non-UK banks in total.*

Supranational Bonds – *a maximum sum of £20m*

Money Market Funds – *a limit of £40m in all MMFs is to be applied at all times.*

Investment management

Counterparties – all investments will be limited to institutions based on the adopted criteria. A schedule of eligible counterparties will be maintained. Their credit ratings and other relevant information will be analysed and monitored on a regular basis by the City Council and its advisors, to ensure the security of monies invested.

Maximum sums - total investments with individual counterparties, groups, non-UK institutions and Money Market Funds, as detailed in **Table** 4, will apply at all times.

Liquidity - the maximum period for any deposit will be 2 years. For investments with non-UK institutions, a maximum period of 364 days will apply. In order to maintain liquidity and reduce the associated risk, the average period for investments will be monitored and reported on a regular basis.

Return – within the criteria detailed above, an appropriate return will be sought.

Reporting – details of the investment portfolio, use of counterparties and the rates of return will be included in all reports to the Audit Committee and Executive Board. In addition, regular monthly reports will be provided to the Treasury Management Panel.

7. Reporting Process

Following approval of the Treasury Management Strategy for 2011/12, the reporting of activity and performance during the year will be, as a minimum:

- A mid-year report to Audit Committee, Executive Board and Council
- An outturn report to Audit Committee, Executive Board and Council

Any required changes to the Strategy, or the associated Prudential Indicators, will be reported to a meeting of the full City Council for consideration for approval, in accordance with CLG guidance. The Treasury Management Panel (comprising the CFO, Director of Strategic Finance, Head of Corporate and Strategic Finance, Treasury Management Officer and other senior finance colleagues) will scrutinise regular reports on treasury management activity throughout the year.

8. Training

The revised Code requires the CFO to ensure that all councillors tasked with treasury management responsibilities, including scrutiny of the treasury management function, receive training appropriate to their needs and understand fully their roles and responsibilities.

With Council elections scheduled for May 2011, a co-ordinated finance training scheme, including treasury management, is under development and will be made available to all councillors, as required, following the election.

9. Management of Risk

Risk management plays a fundamental role in treasury activities, due to the value and nature of transactions involved. **Appendix B** details the specific risks identified in respect of treasury management within the City Council and the adopted Risk Management Action Plan. This Plan is reviewed at regular intervals at meetings of the Treasury Management Panel.

PRUDENTIAL INDICATORS 2009/10 – 2013/14					
	2009/10 Actual £m	**2010/11 Est £m**	**2011/12 Est £m**	**2012/13 Est £m**	**2013/14 Est £m**
1. PRUDENCE INDICATORS					
i) Capital Expenditure					
General Fund	165.056	150.440	103.256	55.656	19.557
HRA	51.527	60.836	25.332	18.271	5.700
	216.583	**211.276**	**128.588**	**74.377**	**25.257**
ii) CFR at 31 March					
General Fund	281.352	304.765	312.790	307.921	295.147
PFI-related debt	165.519	265.512	259.196	271.574	263.906
HRA	284.800	321.777	321.075	320.373	319.671
	731.670	**892.054**	**893.061**	**899.868**	**878.724**
iii) External Debt at 31 March					
Borrowing	501.227	534.746	542.046	581.475	612.999
Other (PFI debt)	165.519	265.512	259.196	271.574	263.906
	666.746	**800.258**	**801.242**	**853.049**	**876.905**
2. AFFORDABILITY INDICATORS					
i) Financing costs ratio					
General Fund	6.08%	7.12%	8.95%	9.33%	9.57%
HRA	14.52%	12.09%	12.18%	12.14%	12.19%
ii) Impact of capital investment decisions					
Council Tax Band D (per annum)	-	-	£0.00	£0.00	£0.00
HRA rent (per week)	-	-	£0.00	£0.00	£0.00
	£m	**£m**	**£m**	**£m**	**£m**
iii) Authorised limit for external debt	-	815.258	831.242	883.049	906.905
iv) Operational Boundary for external debt	-	815.258	821.242	873.049	896.905
3. TREASURY MANAGEMENT INDICATORS					
i) Limit on variable interest rates	0-20%	0 – 50%	0 – 50%	0 – 50%	0 – 50%
ii) Limit on fixed interest rates	80-100	50–100%	50–100%	50–100%	50–100%
iii) Fixed Debt maturity structure					
- under 12 months	0-20%	0 – 20%	0 – 20%	0 – 20%	0 – 20%
- 12 months to 2 years	0-20%	0 – 20%	0 – 20%	0 – 20%	0 – 20%
- 2 to 5 years	0-50%	0 – 25%	0 – 25%	0 – 25%	0 – 25%
- 5 to 10 years	0-75%	0 – 25%	0 – 25%	0 – 25%	0 – 25%
- 10 to 25 years		0 – 50%	0 – 50%	0 – 50%	0 – 50%
- 25 to 40 years	25-100%	0 – 25%	0 – 25%	0 – 25%	0 – 25%
- 40 years and above		0 – 75%	0 – 75%	0 – 75%	0 – 75%
iv) Sums invested for >364 days					
- in-house limit	£25m	£40m	£60m	£60m	£60m
v) Adoption of the *CIPFA Code of Practice for Treasury Management in the Public Services*	Yes	Yes	Yes	Yes	Yes

See overleaf for notes to the above table.

NOTES TO THE SCHEDULE OF PRUDENTIAL INDICATORS

1) **<u>Prudence Indicators</u>**

i) *'Estimate of total capital expenditure'* – a "reasonable" estimate of total capital expenditure to be incurred in the next 3 financial years, split between the General Fund and the Housing Revenue Account (HRA).

- This estimate takes into account the City Council's asset management and capital investment strategies.

ii) *'Capital financing requirement' (CFR)* – this figure constitutes the aggregate amount of capital spending which has not yet been financed by capital receipts, capital grants or contributions from revenue, and represents the City Council's underlying need to borrow money long-term. An actual figure at 31 March each year is required, together with estimates for the next three financial years.

- This approximates to the previous Credit Ceiling calculation and provides an indication of the total long-term debt requirement.
- From 31 March 2010, the CFR includes an estimation of the total debt which will be brought 'on-balance sheet' in respect of PFI schemes previously not accounted for.

iii) *'External debt'* - the actual level of gross borrowing (plus other long-term liabilities) calculated from the balance sheet, with estimates for the next three financial years. (From 31 March 2010, the figures include the debt relating to on-balance sheet PFI schemes).

2) **<u>Affordability Indicators</u>**

i) '*Ratio of financing costs to net revenue stream'* – expresses the revenue costs of the City Council's borrowing (interest payments and provision for repayment) as a percentage of the total sum to be raised from government grant, business rates and council tax (General Fund) and housing subsidy and rent income (HRA).

- These indicators show the impact of borrowing on the City Council's revenue accounts and enable a comparison between years to be made. At present, the cost of borrowing is supported by Central Government through the Revenue Support Grant and Housing Subsidy systems, although this may not always be the case in the future.

ii) *'Incremental impact of capital investment decisions'* – expresses the revenue consequences of future capital spending plans to be met from unsupported borrowing on both the level of council tax and weekly housing rents.

- This is a key indicator, which provides a direct link between the City Council's capital programme and its revenue budget and enables the revenue impact of additional unsupported capital investment to be understood.

iii) *'Authorised limit for external debt'* – this represents the maximum amount that the City Council may borrow at any point during the year and replaces the previous 'overall external borrowing' limit. An estimate for the next three financial years is required.

- This figure allows for the possibility that all borrowing for capital purposes may be undertaken early in the year, with a further sum to reflect any temporary borrowing as a result of adverse cash flow. This represents a 'worst case' scenario and the level is very unlikely to be reached.

iv) *'Operating boundary for external debt'* – this indicator is a working limit and represents the highest level of borrowing that the City Council is expecting to reach at any time during the year

- It is recognised that this operational boundary may be breached in exceptional circumstances. However, the Prudential Code recommends that a sustained pattern of borrowing above this limit be investigated as a potential symptom of a more serious financial problem.

3) **<u>Treasury Management Indicators</u>**

i) *'The amount of net borrowing which is at a variable rate of interest'* - expressed either as an absolute amount or a percentage. Upper and lower limits for the next three financial years are required.

- High levels of variable rate debt leaves the City Council at risk from increases in interest rates. This figure represents the maximum permitted exposure to such debt.

ii) *'The amount of net borrowing which is at fixed rate of interest'* - expressed either as an absolute amount or a percentage. Upper and lower limits for the next three financial years are required.

- Fixed rate borrowing provides certainty for future interest costs, regardless of movements in interest rates. The lower limit is effectively the counterpart to the upper limit for variable rate borrowing.

iii) *'Upper and lower limits with respect to the maturity structure of the authority's borrowing'* – this shows the amount of fixed rate borrowing maturing in each period, expressed as a percentage of total fixed rate borrowing.

- This indicator is designed to be a control over the City Council having large amounts of fixed rate debt falling to be replaced at the same time.

iv) *'Total sums invested for periods of greater than 364 days* – a limit on investments for periods longer than 1 year. A three-year estimate is required.

- This indicator is designed to protect the liquidity of investments, ensuring that large proportions of the City Council's cash reserves are not invested for long periods.

v) *The adoption of the CIPFA Code of Practice for Treasury Management in the Public Services'.* This is not a numerical indicator, but a statement of good practice.

- Nottingham City Council adopted the Code on 18 February 2002. The revised Code, issued in 2009, has been incorporated within the City Council's adopted strategy and procedures.

APPENDIX B

Risk Management Action Plan (RMAP)

Likelihood	
1	Remote
2	Unlikely
3	Possible
4	Likely
5	Almost Certain

Likelihood (L)					
5	5	10	15	20	25
4	4	8	12	16	20
3	3	6	9	12	15
2	2	4	6	8	10
1	1	2	3	4	5
	1	2	3	4	5
	Impact (I)				

Impact	
1	Negligible
2	Minor
3	Moderate
4	Major
5	Catastrophic

Low Seriousness	Medium Seriousness	High Seriousness

Summary Business Risk: SRR17 – Failure to protect Council's investments			
Owned by: DCEX/CD - Resources	Completed by: DCEX/CD - Resources	Completed: October 2010	Next Review: April 2011
Prevailing Summary risk Threat Level (LxI)	6 (average) (2 x 3.0)	Target summary Risk Threat Level	4 (2x2)
Summary risk mitigation effectiveness (Effective, yet to secure improvement, may not be enough)		Effective	

Risks under risk management:

Risk Ref:	**Description**	**Current Risk Rating Score (LxI)**	**Target Risk Rating Score (LxI)**
1	Inappropriate investment of monies with counterparties	1 x 4 = 4	1 x 3 = 3
2	Inappropriate investment strategy	2 x 3 = 6	2 x 3 = 6
3	Inappropriate borrowing strategy	2 x 3 = 6	2 x 2 = 4
4	Inappropriate management of debt portfolio	2 x 3 = 6	2 x 2 = 4
5	Poor cash management	2 x 3 = 6	2 x 2 = 4
6	Colleague fraud	2 x 3 = 6	2 x 2 = 4
7	Failure to comply with CIPFA Code of Practice and/or respond to changes in relevant legislation	2 x 3 = 6	1 x 3 = 3

<table>
<tr><th colspan="9">Current Management Action / Controls Acting on Risk?
Delete as applicable: Some None</th></tr>
<tr><th rowspan="2">Risk Ref.</th><th rowspan="2">Current Management/actions in place</th><th rowspan="2">Adequacy of action/control to mitigate risk</th><th rowspan="2">Additional management action/ controls</th><th colspan="2">Responsibility for additional action</th><th rowspan="2">Critical success factors of additional actions</th><th colspan="2">Key Dates</th></tr>
<tr><th>CD</th><th>D/ HoS</th><th>Additional controls complete</th><th>Progress review frequency</th></tr>
<tr><td>1.</td><td>• Continued use of new external advisors – Arlingclose
• Use of approved counterparties list based on fuller range of formal credit ratings and wider market intelligence and advice of new advisors
• Limits set for amounts and time periods with individual institutions
• Limits for counterparties amended as and when required
• Checks introduced arising from the review continue and are successful.
• New TM and investment strategy recently reviewed and implemented
• Regular review takes place of the success</td><td>EFFECTIVE</td><td>• Maintain current arrangements
• Internal audit activity programmed</td><td>CME</td><td>TK/JA</td><td>• Weekly check by Deputy S151 officer of current investments continues to take place.
• Internal audit report findings are strong
• TM panel continues to meet regularly to review the overall position.
• Implementation of revised TM and investment strategies when appropriate</td><td>Ongoing

Ongoing

Ongoing

Ongoing</td><td>Ongoing

At least quarterly and as required

Subject to regular review

As req’d</td></tr>
</table>

	of the TM and investment strategies. • Continued scan of wider economic environment and action taken.							
2.	• Retention of new external advisors. • Regular reviews of interest rate forecasts • Knowledge of investment products through attending seminars • Regular review of the investment and TM strategies • Constant scanning of wider economic activity and prompt response • All funds with counterparties that were reclassified have now been returned in full with interest • Second dividend from Icelandic banks has been received. • Testing of the system took place and enabled further strengthening actions to be implemented. • CFO takes action	EFFECTIVE		CME	TK/JA	• TM colleagues continue to work with advisors and colleagues to keep abreast of wider economic conditions and respond accordingly. • TM panel continues to meet regularly to review the overall position and specifics where required. • Training continues to take place.	Ongoing ongoing As req'd	Quarterly At least quarterly and as required

	under delegation (and in consultation with portfolio holder) to respond quickly to emerging issues. • Linked in with LGA work on recovery of funds in Icelandic banks. • Ongoing regular review (at least quarterly) with formal changes implemented where required.							
3.	• Identification and monitoring of annual borrowing requirement • Monitoring of borrowing rates • Use of alternative products • Regular review of arrangements and possibilities • Fundamental review of capital programme has taken place and will inform a new capital strategy.	EFFECTIVE – except for Capital Programme review element – YET TO SECURE IMPROVEMENT	• Capital programme review completed. • New capital strategy to be written • Maintain all other current arrange-ments	CME	TK/JA JA	• Sufficient resource to cover capital expenditure and cashflows • Continued regular review by TM panel. • Approval of new Capital Strategy by Exec Board		Quarterly + as req'd Spring 2010
4	• Retention of new external advisors – Arlingclose • Regular monitoring of debt maturity profile	EFFECTIVE	• Maintain existing arrange-ments	CME	TK/JA	• Continued regular review by TM panel	At TM panel meetings	Quarterly

	• Opportunities for rescheduling identified and implemented							
5	• Use of cash forecasting models, with regular monitoring and updates undertaken • Track record is sound • Continuous adaptation of model in the light of prevailing and forecast circumstances	EFFECTIVE	• Maintain existing arrange-ments	CME	TK/JA	• Regular review by TM panel	At TM panel meetings	At least Quarterly
6	• Delegation and approved process in place • Separation of duties between treasury management dealing and accounting • Annual internal audit review • Use of professional indemnity insurance • Governance checks in place – e.g.: review by deputy s151 officer and TM Panel in place and satisfactory outcomes to date • System test took place	EFFECTIVE	• A periodic system test to take place going forward • Maintain existing arrangements – to be changed if testing identifies any issues	CME	TK/JA	• Satisfactory outcome of internal audit review • Continuing satisfactory outcome of checks by deputy s151 officer and system tests. • TM Panel review is robust	Internal audit report TBD. Ongoing TM Panel meetings	Quarterly Ongoing Ongoing
7	• Formal adoption of	EFFECTIVE	• Existing	CME	TK/JA	• Continued		

	Code in place since inception. • Updates are reflected in annual review of TM and Investment Strategies • Review of requirements to take place as early as possible • Training on accounting issues		arrange-ments to continue			application of current arrangements • Revisions are promptly and accurately reflected • Satisfactory internal audit review outcome • Robust appraisal by TM panel	Ongoing Annual TM and investment strategy Audit report TM Panel meetings	Ongoing Annual TBD At least quarterly

APPENDIX C

GLOSSARY OF TREASURY MANAGEMENT TECHNICAL TERMS	
TERM	**DEFINITION**
Bank Rate	The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate".
Capital Expenditure	Expenditure on the acquisition, creation or enhancement of capital assets.
Capital Financing Requirement (CFR)	The Council's underlying need to borrow for capital purposes representing the cumulative capital expenditure of the local authority that has not been financed.
Capital Receipts	Money obtained on the sale of a capital asset.
CNAV	Constant Net Asset Value - a term used in relation to the value of 1 share in a fund. The value of a share is always £1.
Credit Default Swaps	A financial instrument for swapping the risk of debt default; the buyer effectively pays a premium against the risk of default.
Credit Rating	A formal opinion issued by a registered rating agency of a counterparty's (or a country's) future ability to meet its financial liabilities; these are opinions only and not guarantees.
Credit Support Scheme	Part of the measures announced by the UK Government on 8 October 2008 to ensure the stability of the financial system. The measures were intended to provide sufficient liquidity in the short term; to make available new capital to UK banks and building societies to strengthen their resources, permitting them to restructure their finances, while maintaining their support for the real economy; and to ensure that the banking system has the funds necessary to maintain lending in the medium term. Institutions that are permitted access to the scheme are termed 'Eligible Institutions'.
Debt maturity	The date when an investment or loan is scheduled to be repaid.
Debt maturity profile	An analysis of the maturity dates of a range of loans/investments.
Diversification	The spreading of investments among different types of assets or between markets in order to reduce risk.
European Investment Bank (EIB)	A non-profit bank created by the European Union principally to make or guarantee loans to EU members for projects contributing to regional development within the Union. Funding is raised through the issuance of bonds, guaranteed by member states.
Government Gilts	Bonds issued by the UK Government. They take their name from 'gilt-edged': being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.
International Financial Accounting Standards (IFRS)	Guidelines and rules set by the International Accounting Standards Board that companies and organisations follow when compiling financial statements.
Money Market Funds (MMF)	Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity.
Minimum Revenue Provision	An annual provision that the Authority is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets
Non-Specified Investments	Term used in the Communities and Local Government Guidance. It includes any investment for periods greater than one year or those with bodies that do not have a high credit rating, use of

	which must be justified.
Pooled funds	Funds in which several investors collectively hold units or shares. The assets in the fund are held as part of a pool.
Premiums and Discounts	A penalty or payment arising from the premature repayment of debt. The calculation is dependant on the relative level of interest rates for the existing loan and current market rates.
Prudential Indicators	Statutory financial indicators derived from treasury management activities which seek to provide insights into the financial impact of the adopted strategy over a period of time.
Private Finance Initiative	A way of funding major capital investments, without immediate recourse to the public purse. Private consortia are contracted to design, build, and in some cases manage new projects. Contracts can typically last for 30 years, during which time the asset is leased by a public authority.
Prudential Code	Developed by CIPFA as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.
Prudential Indicators	Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators.
PWLB	Public Works Loans Board. A statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.
Quantitative Easing	The process used by the Bank of England to directly increase the quantity of money in the economy. The Bank buys assets from private sector institutions and credits the seller’s bank account. The seller has more money in their bank account, while their bank holds a claim against the Bank of England (known as reserves). The end result is more money out in the wider economy.
Revenue Expenditure	Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.
SORP	Statement of Recommended Practice for Accounting (Code of Practice on Local Authority Accounting in the United Kingdom).
Specified Investments	Term used in the CLG Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than 1 year. UK government, local authorities and bodies that have a high credit rating.
Supranational Bonds	Debt issued by international organisations such as the World Bank, the Council of Europe and the European Investment Bank
Supported Borrowing	Borrowing for which the costs are supported by the government or third party.
Treasury Management Code	CIPFA’s Code of Practice for Treasury Management in the Public Services.
Term Deposits	Deposits of cash with terms attached relating to maturity and rate of return (interest).
Unsupported Borrowing	Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing.