CITY COUNCIL - 12 DECEMBER 2011

REPORT OF THE DEPUTY LEADER

TREASURY MANAGEMENT – 2011/12 HALF YEARLY REPORT AND PROPOSED INVESTMENT STRATEGY CHANGES

1 SUMMARY

1.1 This report provides details of treasury management activity to 30 September 2011 and seeks approval for changes to the 2011/12 investment strategy.

1.2 A copy of the report approved by Executive Board on 22 November 2011 is attached as Appendix 1. Within that report are details of treasury management activity (Sections 3.1 to 3.6) and proposals relating to the current investment strategy (Section 3.7).

2 RECOMMENDATIONS

IT IS RECOMMENDED that:

2.1 The treasury management actions taken in 2011/12 to date, detailed in Appendix 1 sections 3.1 to 3.6, are noted.

2.2 The proposed changes to the 2011/12 investment strategy, detailed in Appendix 1 section 3.7, are approved.

3 REASONS FOR RECOMMENDATIONS (INCLUDING OUTCOMES OF CONSULTATION)

3.1 To ensure compliance with the Code of Practice on Treasury Management in Public Services (the Code) adopted by the City Council in February 2002.

4 OTHER OPTIONS CONSIDERED IN MAKING RECOMMENDATIONS

4.1 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 our debt whilst maintaining an even debt profile in future years, and to maximise investment returns within stated security and liquidity guidelines.

5 BACKGROUND

5.1 Treasury management is the management of the organisation's cash flows, including its borrowings and investments. It is regulated by the Code of Practice.

5.2 Any changes to the treasury management strategy during the financial year are required to be reported to and approved by a full meeting of the Council.

5.3 On 22 November 2011, Executive Board considered a report on treasury management activity to 30 September 2011. Executive Board noted the activity and endorsed for approval further revisions to the 2011/12 investment strategy.

6 FINANCIAL IMPLICATIONS (INCLUDING VALUE FOR MONEY)

6.1 There are no direct financial implications or value for money issues arising from this report.

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.

8 EQUALITY IMPACT ASSESSMENT (EIA)

8.1 An EIA has not been carried out as there are no proposals for new or changing policies, services or functions.

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

9.1 Treasury management working papers.

10 PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

10.1 Executive Board report and minutes, 22 November 2011

COUNCILLOR GRAHAM CHAPMAN
DEPUTY LEADER

APPENDIX 1

EXECUTIVE BOARD – 22 NOVEMBER 2011

<table>
<tr><td>Title of paper:</td><td colspan="2">TREASURY MANAGEMENT 2011/12 – HALF YEARLY UPDATE</td></tr>
<tr><td>Director(s)/ Corporate Director(s):</td><td>Carole Mills-Evans
Deputy Chief Executive & Corporate Director, Resources</td><td>Wards affected:
All</td></tr>
<tr><td>Portfolio Holder(s):</td><td>Councillor Graham Chapman, Portfolio Holder for Resources, Economic Development and Reputation</td><td>Date of consultation with Portfolio Holder(s):
31 October 2011</td></tr>
<tr><td>Report author and contact details:</td><td colspan="2">Jeff Abbott, Head of Corporate and Strategic Finance
Tel: 0115 8763648
E-mail: jeff.abbott@nottinghamcity.gov.uk</td></tr>
<tr><td>Other colleagues who have provided input:</td><td colspan="2">Pete Guest, Treasury Management Officer
Tel: 0115 8764163
E-mail: pete.guest@nottinghamcity.gov.uk</td></tr>
<tr><td colspan="3"></td></tr>
<tr><td>Key Decision:</td><td colspan="2">No</td></tr>
<tr><td colspan="3">Reasons for Key Decision:</td></tr>
<tr><td colspan="2">Expenditure of £1,00,000 or more in a single year</td><td></td></tr>
<tr><td colspan="2">Revenue income of £1,00,000 or more in a single year</td><td></td></tr>
<tr><td colspan="2">Savings of £1,00,000 or more in a single year</td><td></td></tr>
<tr><td colspan="2">Capital expenditure of £1,000,000 or more</td><td></td></tr>
<tr><td colspan="2">Capital income of £1,000,000 or more</td><td></td></tr>
<tr><td colspan="2">To be significant in terms of its effects on communities living or working in an area consisting two or more wards in the City</td><td></td></tr>
<tr><td colspan="3"></td></tr>
<tr><td colspan="3">Relevant Council Plan Strategic Priority:</td></tr>
<tr><td colspan="2">World Class Nottingham</td><td>✓</td></tr>
<tr><td colspan="2">Work in Nottingham</td><td>✓</td></tr>
<tr><td colspan="2">Safer Nottingham</td><td>✓</td></tr>
<tr><td colspan="2">Neighbourhood Nottingham</td><td>✓</td></tr>
<tr><td colspan="2">Family Nottingham</td><td>✓</td></tr>
<tr><td colspan="2">Healthy Nottingham</td><td>✓</td></tr>
<tr><td colspan="2">Leading Nottingham Better</td><td>✓</td></tr>
<tr><td colspan="3"></td></tr>
<tr><td colspan="3">Summary of issues (including benefits to citizens/service users):</td></tr>
<tr><td colspan="3">This report sets out treasury management actions and performance from 1 April 2011 to 30 September 2011 and seeks endorsement of changes to the current investment strategy.</td></tr>
<tr><td colspan="3"></td></tr>
<tr><td colspan="3">Recommendation(s):</td></tr>
<tr><td>1</td><td colspan="2">To note the treasury management actions taken in 2011/12 to date, specifically that:
No new long-term borrowing or debt rescheduling has been undertaken to date
The average return on investments to 30 September 2011 was 1.08%
Between 1 April and 30 September, daily cash flow performance was above target at 98.5%</td></tr>
<tr><td>2</td><td colspan="2">To endorse and recommend for approval by the City Council at its meeting on 12 December 2011 further revisions to the investment strategy for 2011/12, detailed in section 3.7 of this report.</td></tr>
</table>

1 BACKGROUND

1.1 Treasury management is the management of the local authority's cash flows, borrowings and investments, together with the management of the associated risks and the pursuit of the optimum performance or return consistent with those risks. Since 1 April 2004 local authorities have been required to have regard to the Prudential Code. The Code requires treasury management to be carried out in accordance with good professional practice. The City Council retains external advisors to assist with this activity.

1.2 In respect of external investments, the City Council is also required to ensure that CLG guidance is followed, with priorities being:

- security of the invested capital
- liquidity of the invested capital and
- commensurate with security and liquidity, an optimum return on those investments.

1.3 The City Council regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of its treasury management activities will be measured. Treasury management risks are identified in the Council's approved Treasury Management Practices. The main risks to the Council's treasury activities are:

- liquidity risk (inadequate cash resources)
- market or interest rate risk (fluctuations in interest rate levels and thereby in the value of investments)
- inflation risks (exposure to inflation)
- credit and counterparty risk (security of investments)
- refinancing risks (impact of debt maturing in future years)
- Legal and regulatory risk (i.e. non-compliance with statutory and regulatory requirements, risk of fraud).

2 REASONS FOR RECOMMENDATIONS (INCLUDING OUTCOMES OF CONSULTATION)

2.1 To ensure that councillors are kept informed of the actions taken by the Chief Finance Officer (CFO) under delegated authority. The current Treasury Management Code of Practice, adopted by the City Council, requires the CFO to submit a minimum of three reports on treasury management each year; a policy and strategy statement for the ensuing financial year, a 6-monthly progress report and an outturn report. It is also a requirement of the Code that the reports be considered by the main City Council meeting, as well as any relevant scrutiny or executive committees.

3 TREASURY MANAGEMENT ACTIVITY TO 30 SEPTEMBER 2011

3.1 <u>2011/12 strategy</u>
The overall Treasury Management Strategy for 2011/12 was approved by the City Council on 7 March 2011. Amendments to the strategy were approved at subsequent meetings on 12 September 2011 and 10 October 2011.

Table 1 shows the actions taken as at 30 September 2011 against each of the main four elements of the strategy:

TABLE 1: TREASURY MANAGEMENT ACTIONS	
Strategy 2011/12	**Actions to 30 September 2011**
New borrowing – to raise up to £19.3m to finance new capital expenditure in the year and replace maturing long-term debt.	To date, no new debt has been raised. (*see 3.3*)
Debt rescheduling – to give consideration to any debt rescheduling or repayment opportunities which enable revenue savings to be generated in the year.	To date no debt rescheduling has taken place (*see 3.4*)
Investments – to ensure the security of funds invested through the application of a restricted counterparty list and a maximum period of investment. Within those confines, to maximise the return on investments.	The average return on investments from 1 April to 30 September 2011 has been 1.08%. The average 7-day LIBID rate (the benchmark) for the same period was 0.47%. The 2010/11 budget assumed an average return of 1.22% for the period. (*see 3.5)*
Daily cash management – to maintain an overnight cash balance between £0.3m overdrawn and £0.15m in-hand every day. The 2011/12 target is to exceed 98.3% (2010/11 performance)	Between 1 April and 30 September 2011 performance was above target, at 98.5%.

3.2 Interest rates during 2011/12

The Bank of England Base Interest Rate of 0.50% has been unchanged in 2011/12. The original strategy report anticipated that rates would increase to 1.25% by March 2012, as the UK economy recovered. However, with growth recovery in the UK continuing to fall below the forecast set by the Government at the start of the year, the current forecast is for any increase in the base interest rate to be deferred to the autumn of 2012 at the earliest.

As a consequence of the above, short term interest rates have remained lower than forecast throughout the first half of 2011/12. Long term interest rates have been impacted by economic uncertainty and in particular as a result of the ongoing European debt crisis. UK gilts have been perceived as a safe haven for investment, driving down yields and therefore borrowing rates. Public Works Loan Board (PWLB) interest rates for all periods from 1 year to 50 years have fallen steadily since the start of the financial year.

Table 2 overleaf shows a range of interest rates over the period and for comparison purposes the forecasted level of interest rates at 1 October 2011 included in the original strategy report are also shown:

TABLE 2: INTEREST RATES 2011/12								
Date	**Base Rate**	**1 month**	**3 month**	**6 month**	**1 year**	**5 years**	**20 years**	**50 years**
	%	**%**						
1 Apr	0.50	0.66	0.73	1.13	1.95	3.65	5.33	5.29
1 May	0.50	0.53	0.73	1.09	1.65	3.36	5.12	5.08
1 Jun	0.50	0.55	0.73	1.09	1.64	3.21	5.07	5.08
1 Jul	0.50	0.54	0.81	1.07	1.64	3.17	5.24	5.26
1 Aug	0.50	0.54	0.81	1.09	1.53	2.74	4.95	5.03
1 Sep	0.50	0.60	0.87	1.17	1.47	2.54	4.68	4.87
1 Oct	0.50	0.62	0.94	1.23	1.49	2.35	4.27	4.62
1 Oct est	***0.75***	***0.90***	***1.20***	***1.50***	***2.25***	***3.25***	***5.00***	***4.75***

3.3 Long-term borrowing

The low return on short-term investments, coupled with a more benign forecast for long term interest rates, has led to a continued deferral in the raising of long-term borrowing, with a combination of internal cash balances and temporary borrowing being used as a source of finance. To date, there has been no new long term borrowing in 2011/12.

3.4 Debt rescheduling

The opportunities for debt rescheduling during 2011/12 have been limited. Low interest rates mean that the repayment of existing long-term debt incurs financial penalties that mitigate against such action.

3.5 Investments

The City Council's cash investments represent reserves and provisions held within the balance sheet plus surplus working capital. As at 30 September 2011, all investments were managed in-house. The 2011/12 budget assumed an average cash surplus of £119.6m during the year. The actual average cash balance to 30 September was £146.4m, largely because the level of reserves and provisions at the 1 April 2011 was higher than estimated.

The average rate of interest earned on all investments to 30 September was 1.08%. The original budget assumed a return of 1.22% for the same period. The fall in return reflects lower short term interest rates and the maintenance of a more cautious investment portfolio, with liquidity (access to monies at short notice) being a key factor in investment decisions. For comparison purposes, the benchmark 7-day LIBID interest rate for the same period was 0.47%.

3.6 2011/12 Investment strategy

The 2011/12 approved investment strategy allows for investments with the following counterparties; the Government's Debt Management Office, other local authorities, UK and overseas banks meeting the required criteria in respect of credit ratings etc, Money Market Funds (pooled, short maturity, high quality investment vehicles offering instant access) and Supranational Bonds. The adoption of specific counterparties is based on a wide range of criteria, including credit ratings, credit default swap rates, government support mechanisms and parent bank support.

During the year, monitoring of the financial position of counterparties is undertaken by both treasury management colleagues and our retained treasury management advisors. This review considers individual credit ratings, credit default swap prices, share prices, changes in sovereign state credit ratings and more general developments in financial markets and the global economy. This then informs decisions to revise the investment strategy to ensure that the Council is well placed to manage any emerging and/or potential risks. As a result, there have been a number of occasions in 2011/12 when existing investment counterparties have been suspended or had individual limits amended as follows:

- Clydesdale Bank (UK) – counterparty suspended, following downgrading of credit rating of parent bank, National Australia Banking Group (18 May).
- UK institutions – maximum period for all new investments reduced from 2 years to 1 year, following market concerns regarding the increased potential of a default by Greece in respect of its sovereign debt (3 August).
- Santander UK (UK) – maximum period for new investments with counterparty reduced to 3 months because of possible credit rating downgrade relating to problems with Spanish parent bank (11 August).
- Societé General (France) – counterparty suspended because of negative market sentiment (11 August).
- All counterparties – maximum period for all new investments reduced to 6 months for UK, US, Canadian and Australian banks, and 1 month for European banks, following further volatility in financial and equity markets (11 August).
- Royal Bank of Scotland and Nationwide Building Society – suspended, following long term rating downgrade by Moodys (7 October).
- Lloyds TSB – suspended, following long term rating downgrade by Fitch (13 October).

Our advisors' view remains that there are no fundamental solvency issues with any of the existing counterparties, but it was considered prudent to make the above changes to the list of eligible institutions and to seek to reduce the average maturity profile of the investment portfolio. The financial position continues to be monitored, with further changes to be implemented if and when market conditions change. Such temporary changes are discussed with the Portfolio Holder as issues arise during the year.

3.7 Further investment strategy changes

As a consequence of the suspension of Clydesdale Bank and other restrictions, a proposal to increase the maximum sum in Money Market Funds (AAA-rated instant access deposits) from £40m to £80m was approved at a meeting of the City Council on 10 October 2011, with an individual limit of £10m per Fund. The existing requirement for all Funds to have a credit rating of AAA and a Constant Net Asset Value (preserving the principal value of the sum invested) was retained.

Following the downgrading of RBS, Nationwide Building Society and Lloyds TSB in October, these institutions were suspended from the Council's approved investment counterparty list. This has added further pressure to the external investment of surplus cash. Whilst the use of the Government's Debt Management Office remains a safe investment 'option of last resort', the low rate of return from such deposits has led to consideration of a further review of the investment strategy.

Currently, UK banks and building societies whose long-term credit rating fell below A+ no longer met the Council's required minimum level for investment. It is considered, however, that the financial strength of such institutions remains fundamentally the same. The downgrade reflects anticipation by rating agencies of the reduced likelihood of government support for organisations that get into financial difficulties in the future. However, these organisations remain systemically important to the UK banking system. Therefore, it is proposed to introduce a further category for counterparties, with a reduced maximum investment period:

UK banks with a minimum short-term rating of F1 (Fitch), A-1 (S&P) or P-1 (Moodys) and a minimum long-term rating of A- (Fitch and S&P) or A3 (Moodys) - investments for a maximum period of 3 months.

The Council's external treasury management advisors have been consulted and consider the above approach to be a reasonable one for the remainder of the financial year. **Appendix A** provides details of the proposed revised investment strategy, together with a schedule of eligible counterparties, including individual limits. This proposal is conditional on endorsement by Executive Board and approval by City Council.

A further detailed review of investment criteria for counterparties will be included in the development of the 2012/13 treasury management strategy, to be reported to the appropriate Boards and Committees early next year.

3.8 Icelandic Bank deposits – update

The City Council had £41.6m invested over three Icelandic banks, which collapsed in October 2008. These banks have continued to pass through an administration process to determine the level of payments to be made to the banks' creditors. The latest position in respect of deposits with each bank is:

a) Heritable Bank (original deposit £15.6m) – the administrators continue to realise the assets of the bank and make stage payments to creditors. To date, repayments of principal and interest totalling £10.294m have been received, representing over 64% of the original investment. It is currently estimated that the final sum recovered will be c 90% of the original deposit.

b) Landsbanki Bank (£15m) and Glitnir bank (£11m) – the issue of the creditor status of UK local authority deposits in the administration process has been a matter of legal challenge in respect of both Glitnir and Landsbanki banks. In March 2011, the Icelandic District Court, after a lengthy litigation process, ruled that UK local authorities were to be treated as priority creditors, which would lead to a significantly higher level of repayment. An appeal against this decision was submitted to the Icelandic Supreme Court in September this year. That Court upheld the original decision and it is now anticipated that the level of recovery will be 100% for Glitnir deposits and c 98% for Landsbanki deposits.

4 OTHER OPTIONS CONSIDERED IN MAKING RECOMMENDATIONS

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 our debt whilst maintaining an even debt profile in future years, and to maximise investment returns within stated security and liquidity guidelines.

5 FINANCIAL IMPLICATIONS (INCLUDING VALUE FOR MONEY)

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 HRA. The remaining costs are included within the treasury management section of the General Fund budget. **Table 3** sets out the budget for 2011/12, with the actual for 2010/11 shown for comparison.

DESCRIPTION	Actual 2010/11 £m	Budget 2011/12 £m
External interest	22.979	23.703
Debt repayment provision	13.256	16.631
Prudential borrowing recharge	(1.611)	(1.303)
Investment interest	(1.402)	(1.885)
HRA recharge	(11.949)	(11.629)
Impairment charge	5.373	-
Transfer to/(from) TM reserve	(3.065)	3.310
Net General Fund position	**23.581**	**28.827**

An estimated outturn for 2011/12, together with budgets for 2012/13 through to 2014/15 will be submitted with the treasury management strategy for 2012/13, in February 2012.

6 RISK MANAGEMENT ISSUES (INCLUDING LEGAL IMPLICATIONS, CRIME AND DISORDER ACT IMPLICATIONS)

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.

7 EQUALITY IMPACT ASSESSMENT (EIA)

There are no proposals for new or changing policies, services or functions.

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

PWLB records, working papers

9 PUBLISHED DOCUMENTS REFERRED TO IN COMPILING THIS REPORT

Treasury Management in the Public Services, Code of Practice 2009 – CIPFA
The Prudential Code for Capital Finance in Local Authorities – CIPFA

Revised investment counterparty list, 2011/12 (w.e.f. 12 Dec 2011)

For UK banks, the following minimum criteria will apply:

- 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) – maximum sum £20m, maximum period of investment 6 months.
- 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 A3 (Moodys) – maximum sum £20m, maximum period of investment 3 months.

For non-UK banks, the following minimum criteria will apply:

- 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) – maximum sum £5m, maximum period of investment 3 months.

The interpretation of these various credit ratings is provided as a note to the table below. 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.

The 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.

ELIGIBLE COUNTERPARTIES FOR INVESTMENT FROM 12 DEC 2012				
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***	***3 months***
		Barclays Bank	£20m	6 months
		Co-Operative Bank	No limit	5 days
		Clydesdale Bank	***£20m***	***3 months***
		HSBC Bank	£20m	6 months
		Nationwide Building Society	***£20m***	***3 months***
		Royal Bank of Scotland / Nat West Bank /	***£20m***	***3 months***
		Santander UK	£20m	3 months
	Australia	Australia & NZ Banking Group	£5m	3 months
		Commonwealth Bank of Australia	£5m	3 months
		National Australia Bank Ltd	£5m	3 months
		Westpac Banking Corp.	£5m	3 months
	Canada	Bank of Montreal	£5m	3 months
		Bank of Nova Scotia	£5m	3 months
		Canadian Imp. Bank of Commerce	£5m	3 months
		Royal Bank of Canada	£5m	3 months
		Toronto-Dominion Bank	£5m	3 months
	Finland	Nordea Bank Finland	£5m	3 months
	France	BNP Paribas	Suspended	
		Calyon	Suspended	
		Credit Agricole SA	Suspended	
		Soc Gen	Suspended	
	Germany	Deutsche Bank AG	£5m	3 months
	Netherlands	Rabobank	£5m	3 months
		ING Bank	£5m	3 months
	Sweden	Svenska Handelsbanken	£5m	3 months
	Switzerland	Credit Suisse	£5m	3 months
	USA	JP Morgan	£5m	3 months
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

Credit Rating Definitions

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.

Limiting Factors

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 £80m in all MMFs is to be applied*