

CARLISLE CITY COUNCIL

Report to:- **The Mayor and Members of The City Council**

Date of Meeting:- 04 March 2003

Agenda Item No:-

16(b)

Public	Policy	Delegated Yes
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Accompanying Comments and Statements	Required	Included
Environmental Impact Statement:	No	No
Corporate Management Team Comments:	No	No
Financial Comments:	Yes	Yes
Legal Comments:	No	No
Personnel Comments:	No	No

Title:- **TREASURY MANAGEMENT STRATEGY STATEMENT AND EXTERNAL BORROWING DETERMINATIONS 2003/04**

Report of:- **The Head of Finance**

Report reference:- **FS13/02**

Summary:-

The report sets out the Treasury Management Strategy Statement for 2003/04 in accordance with the requirements of the Revised CIPFA Code of Practice on Treasury Management. Also embraced within the report are the External Borrowing Determinations for 2003/04 as required under the 1989 Local Govt and Housing Act.

Recommendation:-

The Portfolio Holder for Finance and Resources proposes to the City Council that:

- (i) The Treasury Management Strategy Statement for 2003/04 be approved as set out in Appendix A.
- (j) The Treasury Policy Statement as drafted by CIPFA be approved as set out in Appendix B.
- (k) The Treasury Management Practice Statements be noted and approved as set out in Appendix C.
- (l) The External Borrowing Determinations for 2003/04 be approved as set out in Appendix D.

Contact Officer: David Steele

Ext: 7288

CITY OF CARLISLE

To: The Executive
06 February 2003

FS13/02

The Mayor and Members of The City Council
04 March 2003

TREASURY MANAGEMENT STRATEGY STATEMENT AND EXTERNAL BORROWING DETERMINATIONS 2003/04

1. INTRODUCTION

- 1.1 The CIPFA Code of Practice on Treasury Management in Local Authorities was first issued in 1992 and updated in 1996 and more recently in December 2001. The City Council formally adopted the current Code in March 2002.
- 1.2 Under the requirements of the Code, the Council, Board or other appropriate body, will receive each year the following reports:-
 - Annual strategy and plan in advance of the year
 - Annual report after its close.

2. TREASURY MANAGEMENT STRATEGY STATEMENT

- 2.1 As required under the Code, the Treasury Management Strategy Statement for 2003/04 is set out in Appendix A. The annual report on treasury management outturn will be prepared as part of the closure of accounts process.

3. TREASURY POLICY STATEMENT

- 3.1 The new Code also requires each organisation to draw up a much truncated and more strategic Treasury Management Policy Statement (TMPS) incorporating just three clauses and a revised definition of treasury management activities. The Code does not require this statement to be approved by the council, board or other appropriate body.
- 3.2 Due to the late arrival of the current Code in terms of the required financial reporting process prior to 1 April 2002, the TMPS for 2002/03 was based upon the model recommended under the 1996 Code. The new TMPS is set out in Appendix B to this report.

4. TREASURY MANAGEMENT PRACTICES (TMPs)

- 4.1 The 2001 Code also sets out a schedule of 12 categories of Treasury Management Practices together with a brief description of their requirements as set out in the Code. The Code does not require that any TMPs are reported to the Council or its Executive. However it was always the practice when the previous Treasury Policy Statement was issued to include certain especially relevant items for members' information and approval e.g. the investment counter-party list. This practice has been continued within the reporting of the TMPs. Details of these TMPs are set out in Appendix C.

5. EXTERNAL BORROWING DETERMINATIONS 2003/04

- 5.1 As a separate but related issue, the Council is also required to agree the annual borrowing determinations required under the 1989 Local Government and Housing Act. These are included in Appendix D to the report.

6. CONSULTATION

- 6.1 Consultation to Date.
None.

- 6.2 Consultation proposed.
None.

7. STAFFING/RESOURCES COMMENTS

Not Applicable

8. HEAD OF FINANCE COMMENTS

Included within the report

9. LEGAL COMMENTS

Not Applicable

10. CORPORATE COMMENTS

Not Applicable

11. RISK MANAGEMENT ASSESSMENT

- 11.1 Management of risk is one of the guiding principles of the Code.

12. EQUALITY ISSUES

Not Applicable

13. ENVIRONMENTAL IMPLICATIONS

Not Applicable

14. CRIME AND DISORDER IMPLICATIONS

Not Applicable

15. RECOMMENDATIONS

15.1 The Portfolio Holder for Finance and Resources proposes to the City Council that:

- (e) The Treasury Management Strategy Statement for 2003/04 be approved as set out in Appendix A.
- (f) The Treasury Policy Statement as drafted by CIPFA be approved as set out in Appendix B.
- (g) The Treasury Management Practice Statements be noted and approved as set out in Appendix C.
- (h) The External Borrowing Determinations for 2003/04 be approved as set out in Appendix D.

ANGELA BROWN

Head of Finance

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Financial Services
Carlisle City Council
29 January 2003
DKS/CH/FS13-02

CARLISLE CITY COUNCIL
TREASURY MANAGEMENT STRATEGY STATEMENT 2003/04

1. INTRODUCTION

1.1 This Strategy details the expected activities of the Treasury function in the forthcoming financial year. Its production and submission to the Executive and Council is a requirement of the CIPFA Code of Practice on Treasury Management which the Council has adopted. The basis of the Strategy lies in determining the appropriate borrowing and investment decisions that will be required during 2003/04. These decisions will be taken in the light of the anticipated movement in both short and long term interest rates.

1.2 It is a statutory requirement under Section 33 of the Local Government Finance Act 1992, for the Council to produce a balanced budget. In particular, Section 32 requires a local authority to calculate its budget requirement for each financial year to include the revenue costs that flow from capital financing decisions. This therefore means that increases in capital expenditure must be limited to a level whereby increases in charges to revenue from:-

1. increases in interest charges caused by increased borrowing to finance additional capital expenditure, and
2. any increases in running costs from new capital projects

are limited to a level which is affordable within the projected income of the Council for the foreseeable future.

2. CURRENT PORTFOLIO POSITION

2.1 The City Council's current treasury portfolio is made up as follows:

	£000's	£000's	Av Rate %
Fixed Rate Funding PWLB	12,190		8.35
Other	<u>15,142</u>		8.75
		27,332	
Variable Rate Funding PWLB	624		4.0
Other	<u>-</u>		-
		<u>624</u>	
Total Debt		27,956	8.47
Total Investments			
* City of Carlisle Inv Fund	15,000	}	4.10
+ Other Investments	<u>30,000</u>		
		45,000	

* Principally set aside receipts
+ Other balances and cash flows

- 2.2 The past twelve months has seen a radical change in the City Council's outstanding loans portfolio due principally to the LSVT that was completed in December 2002. In a normal transfer, the net proceeds of the sale would have been used to repay the outstanding housing debt. Because the value of the stock was much less than that of the outstanding debt relating to the stock, a total of £17,985,000 PWLB debt was repaid by the Government to clear this 'overhanging debt'.
- 2.3 The City Council's investment portfolio in contrast was not affected by the LSVT process as there was no net capital receipt for the reason stated above. However the City Council still retains the bulk of its 'set aside receipts' together with other revenue and capital balances that together are represented by its total of outstanding investments. It will be noted that in the current financial climate the average yield on investments is presently much lower than that which is being paid on the City Council's outstanding loans.

3. INTEREST RATE PROSPECTS

- 3.1 The City Council has appointed Sector Treasury Services as its treasury adviser and part of their service is to assist in formulating a view on interest rates. The following table shows the current interest rate expectations as forecast by UBS in the next 18 months. This is also Sector's view.

	2002	Current	2003			
	Q4		Q1	Q2	Q3	Q4
	%		%	%	%	%
Repo Rate (Base Rate)	4.00	4.00	4.00	4.00	4.00	4.00
10 Year Gilt	4.50	4.50	4.50	4.50	4.50	4.50
30 Year Gilt	4.25	4.52	4.25	4.25	4.25	4.25

All rates are forecast as at the end of the Quarter. A wider range of forecasts is set out in Appendix A1.

- 3.2 Short term rates are anticipated to remain unchanged at 4% until the end of 2003. Since base rate is already unchanged since November 2001, this forecast would indicate no movement in this rate for over two years. If there is a change in the rate during 2003, it appears more likely to be a reduction occasioned by a fall in share values or a slowdown in economic growth causing a drop in consumer confidence. However the view is that by the end of the year base rate would have returned to 4%.
- 3.3 Long term rates meanwhile have fallen in 2002 as a result of money flowing out of equities into the safer havens of government bonds. Accordingly fixed interest rates have fallen and this has been reflected in lower PWLB rates. With the uncertainties surrounding the stock market and economic growth generally, not to mention possible war with Iraq, this trend looks set to continue in 2003 with a continuation of low yields on government bonds and thus low PWLB rates.

4. LONG TERM BORROWING STRATEGY

- 4.1 The City Council's borrowing requirement for capital purposes in 2003/04 is provisionally estimated as:

	£
Basic Credit Approval	1,153,000
Supplementary Credit Approvals	<u>156,000 (est)</u>
	1,309,000
Add Maturing Debt - PWLB	Nil
- Market	<u>2,000</u>
Gross Borrowing Requirement	1,311,000
Less Principal paid by Borrowing Accounts	138,000 -
Net Borrowing Requirement	<u>£1,173,000</u>

- 4.2 Under current PWLB rates, there is an absolute entitlement to replace any maturing PWLB loan in the year with fresh funds. Credit approvals also enable PWLB funds to be drawn down and hence a PWLB quota of £1.3m can be anticipated for 2003/04.
- 4.3 Additionally the City Council still has the option to borrow up to £4.4m from the PWLB in the remainder of 2002/03 to replace debt that has already matured in the current financial year. There may be merit in replacing at least part of this sum later in 2002/03 on a one year basis which would give the City Council access to additional PWLB quota in 2003/04 that could be used for debt rescheduling. This issue will be discussed with the City Council's treasury advisors in the near future. (See also para 7).
- 4.4 Much of the City Council's outstanding loans portfolio is of fairly long duration at fixed rates and thus there is little risk to the authority from an increase in long term funding rates. Therefore any long term borrowing, whether in the remainder of this year or in 2003/04, is likely to be at the shorter end of the spectrum, i.e. 1-2 years and taken up with more tactical considerations in mind.

5. TEMPORARY INVESTMENT STRATEGY

- 5.1 I would however anticipate that the City Council will continue to be a regular investor in the short-term money market. Whilst it is necessary to allow for retaining a level of liquidity, most short term funds will in practice be invested for fixed periods of up to 364 days, subject to the investment parameters set out in Appendix C. The 2003/04 budget has been framed on an assumed investment rate of 4.1%. Opportunities will therefore be taken whenever practical to secure investment returns in excess of this benchmark although presently all investment rates out to 1 Year are well below this figure. This may therefore predicate a strategy of generally placing funds for shorter periods to secure more attractive yields through compounding of interest. However an element of flexibility in investing funds will be required in case of any unexpected shifts in market sentiment.

- 5.2 All investments will of course be made only in accordance with the Approved Investments Regulations (1990) with subsequent amendments and with those institutions identified in the Council's approved counter-party list.
6. CITY OF CARLISLE INVESTMENT FUND
- 6.1 Approximately £15m of the City Council's investments are managed by external fund managers. As reported to the Executive earlier in the financial year. The Fund will be managed by Morley Fund Management who acquired the local authority investment funds formerly managed by Dresdner RCM Global Investors. The new arrangements for this authority took effect from 1 February 2003. It is as yet too early to gauge the financial performance of Morley although external fund managers might be expected to outperform (albeit marginally) funds managed in house on a medium term (3-5 years) timescale.
- 6.2 The performance of Morley will be closely monitored, both on an absolute basis and also in comparison to the City Council's own in house management of its surplus cash. Normally the Fund is reported on as part of the annual outturn report on Treasury Management which will be presented to the Executive in the summer as required under the Code of Practice.
7. DEBT RESCHEDULING
- 7.1 The issue of debt rescheduling will be kept under review in 2003/04. The prospects for extensive rescheduling do not look very promising at the moment although the very substantial LSVT debt repayment means that any premium payable on a premature repayment of any remaining PWLB debt would be correspondingly reduced. Drawing part of the 2002/03 quota would facilitate any rescheduling. However the prospects of prematurely repaying any of the £15m stock issue at this stage look very remote. Therefore at this stage in the year a 'wait and see' stance seems to be the most appropriate position to take on possible debt rescheduling in 2003/04.
8. CONCLUSION
- 8.1 Each new year brings its own problems and challenges and 2003/04 looks to be no exception. The stock market is now at its lowest level for over seven years and in the current climate of economic downturn and international uncertainty it looks unlikely to recover to any substantial degree in the near future.
- 8.2 Against this background, long-term borrowing rates look likely to remain depressed. The City Council's own long term funding requirement in 2003/04 is relatively modest. However with short-term rates at their lowest level since the 1960s, the greater problem for the City Council is to achieve the anticipated return on its portfolio of investments.
- 8.3 The regular Treasury Management reports that are presented to the Executive will update members on all the above issues.

INTEREST RATE FORECASTS

The data below shows a variety of forecasts published by a number of institutions. The first three are individual forecasts including those of UBS and Capital Economics (an independent forecasting consultancy), who both provide economic forecasts while HSBC are the authority's own bankers. The final two represent summarised figures drawn from the population of all major City banks and academic institutions. The current data shows the rates at the time of issue, not necessarily current rates.

1. INDIVIDUAL FORECASTS

UBS Warburg Economic interest rate forecast (for quarter ends) – December 2002

(%)	Current	Q4 2002	Q1 2003	Q2 2003	Q3 2003	Q4 2003
Base Rate	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
10 Yr Gilt	4.50%	4.50%	4.50%	4.50%	4.50%	4.50%
30 Yr Gilt	4.52%	4.25%	4.25%	4.25%	4.25%	4.25%

Capital Economics interest rate forecast – December 2002

(%)	Current	Q4 2002	Q1 2003	Q2 2003	Q3 2003	Q4 2003
Base Rate	4.00%	4.00%	4.00%	4.00%	3.75%	3.50%
10 Yr Gilt	4.50%	4.60%	4.60%	4.50%	4.40%	4.20%
30 Yr Gilt	4.59%	4.60%	4.60%	4.50%	4.50%	4.40%

HSBC interest rate forecast – October 2002

(%)	Current	Q4 2002	Q1 2003	Q2 2003	Q3 2003	Q4 2003
Base Rate	4.00%	4.00%	4.00%	4.00%	4.00%	4.00%
10 Yr Gilt	4.50%	4.50%	4.50%	4.30%	4.20%	4.20%
30 Yr Gilt	4.52%	4.40%	4.40%	4.40%	4.30%	4.30%

2. SURVEYS OF ECONOMIC FORECASTS

HM Treasury – summary of 35 independent forecasters' views of base rate – as at December 2002 (2003 – 2005 are as at November 2002 but are based on 11 forecasts)

%	2002 Year End	2003 Year End	2004 Average	2005 Average	2006 Average
Average	4.00%	4.34%	5.14%	5.12%	4.81%
Highest	4.50%	5.25%	6.10%	5.60%	5.00%
Lowest	3.75%	2.85%	4.60%	4.90%	4.50%

Consensus Forecasts – summary view of 25 city houses on the likely change in short term and 10 year fixed interest rates (December 2002)

(%)	Dec – 02	Mar – 03	Dec – 03
3 Month Interbank – Average	3.91%	4.00%	4.50%
High	3.91%	4.60%	5.10%
Low	3.91%	3.60%	3.50%
10 Year Gilt Yield – Average	4.52%	4.60%	4.90%
High	4.52%	5.00%	5.40%
Low	4.52%	4.00%	4.30%

TREASURY MANAGEMENT POLICY STATEMENT 2003/04

1. CIPFA recommends that an organisation's treasury management policy statement adopts the following forms of words to define the policies and objectives of its treasury management activities:
 - "1. This organisation defines its treasury management activities as:
"The management of the organisation's 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."
 2. This organisation 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. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation.
 3. This organisation acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. It is therefore committed to the principles of achieving best value in treasury management, and to employing suitable performance measurement techniques, within the context of effective risk management."
2. Whilst the Code does not require that the Treasury Policy Statement is specifically approved by the Executive or Council, the Executive may wish to formally endorse this Statement as part of its approval of the Treasury Strategy Statement for 2003/04.

TREASURY MANAGEMENT PRACTICES

The Code identifies twelve areas where statements of treasury management practices (TMPs) should be developed to implement the full requirements of the Code.

TMP 1	Risk management
TMP 2	Best value and performance measurement
TMP 3	Decision-making and analysis
TMP 4	Approved instruments, methods and techniques
TMP 5	Organisation, clarity and segregation of responsibilities, and dealing arrangements
TMP 6	Reporting requirements and management information arrangements
TMP 7	Budgeting, accounting and audit arrangements
TMP 8	Cash and cash flow management
TMP 9	Money laundering
TMP 10	Staff training and qualifications
TMP 11	Use of external service providers
TMP 12	Corporate governance

The Code does not specifically require that any TMPs need to be approved by the Executive or Council. However the previous Treasury Policy Statement contained much information that is now embraced within the TMPs. The following paragraphs set out the broad content of the TMPs with specific Appendices where appropriate.

TMP1 Risk Management

General Statement

"The Head of Finance will design, implement and monitor all arrangements for the identification, management and control of treasury management risk, will report at least annually on the adequacy/suitability thereof, and will report, as a matter of urgency, the circumstances of any actual or likely difficulty in achieving the organisation's objectives in this respect, all in accordance with the procedures set out in *TMP6 Reporting requirements and management information arrangements*. In respect of each of the following risks, the arrangements which seek to ensure compliance with these objectives are set out in the schedule to this document."

(1) Liquidity Risk Management

"The City Council will ensure it has adequate though not excessive cash resources, borrowing arrangements, overdraft or standby facilities to enable it at all times to have the level of funds available to it which are necessary for the achievement of its business/service objectives."

(2) Interest Rate Risk Management

"The City Council will manage its exposure to fluctuations in interest rates with a view to containing its interest costs, or securing its interest revenues, in accordance with the amounts provided in its budgetary arrangements as amended in accordance with *TMP6 Reporting requirements and management information arrangements*."

(3) Exchange Rate Risk Management

(Not relevant for this authority).

(4) Inflation Risk Management

The effects of varying levels of inflation, insofar as they can be identified as impacting directly on its treasury management activities, will be controlled by the organisation as an integral part of its strategy for managing its overall exposure to inflation.

It will achieve these objectives by the prudent use of its approved financing and investment instruments, methods and techniques, primarily to create stability and certainty of costs and revenues, but at the same time retaining a sufficient degree of flexibility to take advantage of unexpected, potentially advantageous changes in the level or structure of interest rates, exchange rates or inflation. The above are subject at all times to the consideration and, if required, approval of any policy or budgetary implications."

(5) Credit and Counterparty Risk Management

"The City Council regards a prime objective of its treasury management activities to be the security of the principal sums it invests. Accordingly, it will ensure that its counterparty lists and limits reflect a prudent attitude towards organisations with whom funds may be deposited. It also recognises the need to have and will therefore maintain, a formal counterparty policy in respect of those organisations from which it may borrow, or with whom it may enter into other financing arrangements. The proposed schedule for 2003/04 is set out in Appendix C1."

(6) Refinancing Risk Management

"The City Council will ensure that any refinancing arrangements are negotiated, structured and documented, and the maturity profile of the monies so raised are managed, with a view to obtaining offer terms for renewal or refinancing, if required, which are competitive and as favourable to the organisation as can reasonably be achieved in the light of market conditions prevailing at the time.

It will actively manage its relationships with its counterparties in these transactions in such a manner as to secure this objective, and will avoid overreliance on any one source of funding if this might jeopardise achievement of the above."

(7) Legal and Regulatory Risk Management

"The City Council will ensure that all of its treasury management activities comply with its statutory powers and regulatory requirements. It will demonstrate such compliance, if required to do so, to all parties with whom it deals in such activities. In framing its credit and counterparty policy, it will ensure that there is evidence of counterparties' powers, authority and compliance in respect of the transactions they may effect with the organisation, particularly with regard to duty of care and fees charged.

This City Council recognises that future legislative or regulatory changes may impact on its treasury management activities and, so far as it is reasonably able to do so, will seek to minimise the risk of these impacting adversely on the organisation."

(8) Fraud, Error and Corruption, and Contingency Management

"The City Council will ensure that it has identified the circumstances which may expose it to the risk of loss through fraud, error, corruption or other eventualities in its treasury management dealings. Accordingly, it will employ suitable systems and procedures, and will maintain effective contingency management arrangements, to these ends."

(9) Market Risk Management

"The City Council will seek to ensure that its stated treasury management policies and objectives will not be compromised by adverse market fluctuations in the value of the principal sums it invests, and will accordingly seek to protect itself from the effects of such fluctuations."

TMP2 **Best Value and Performance Measurement**

"The City Council is committed to the pursuit of best value in its treasury management activities and to the use of performance methodology in support of that aim, within the framework set out in its treasury management policy statement."

TMP3 **Decision-Making and Analysis**

"The City Council will maintain full records of its treasury management decisions and of the processes and practices applied in reaching those decisions, both for the purposes of learning from the past, and for demonstrating that reasonable steps were taken to ensure that all issues relevant to those decisions were taken into account at the time."

TMP4 **Approved Instruments, Methods and Techniques**

"The City Council will undertake its treasury management activities by employing only those instruments, methods and techniques detailed in Appendix C2 to this document, and within the limits and parameters defined in TMP1 *Risk management*."

TMP5 **Organisation, Clarity and Segregation of Responsibilities, and Dealing Arrangements**

"The City Council considers it essential, for the purposes of the effective control and monitoring of its treasury management activities, for the reduction of the risk of fraud or error, and for the pursuit of optimum performance, that these activities are structured and managed in a fully integrated manner, and that there is at all times a clarity of treasury management responsibilities."

The principle on which this will be based is a clear distinction as far as is feasible between those charged with setting treasury management policies and those charged with implementing and controlling these policies, particularly with regard to the execution and transmission of funds, the recording and administering of treasury management decisions and the audit and review of the treasury management function.

The Head of Finance will ensure that there are clear written statements of the responsibilities for each post engaged in treasury management, and the arrangements for absence cover.

The Head of Finance will ensure there is proper documentation for all deals and transactions, and that procedures exist for the effective transmission of funds.

The delegations to the Head of Finance in respect of treasury management are set out within the terms of the City of Carlisle's Constitution. The Head of Finance will fulfil all such responsibilities in accordance with these delegations and the CIPFA *"Standard of Professional Practice on Treasury Management."*

TMP6 Reporting Requirements and Management Information Arrangements

"The City Council will ensure that regular reports are prepared and considered on the implementation of its treasury management policies; on the effects of decisions taken and transactions executed in pursuit of those policies; on the implications of changes, particularly budgetary, resulting from regulatory, economic, market or other factors affecting its treasury management activities; and on the performance of the treasury management function.

As a minimum, the City Council will receive:

- An annual report on the strategy and plan to be pursued in the coming year
- An annual report on the performance of the treasury management function, on the effects of the decisions taken and the transactions executed in the past year, and on any circumstances of non-compliance with the organisation's treasury management policy statement and TMPs
- Quarterly reports on treasury management transactions"

TMP7 **Budgeting, Accounting and Audit Arrangements**

"The Head of Finance will prepare and the City Council will approve and if necessary from time to time will amend, an annual budget for treasury management, which will bring together all of the costs involved in running the treasury management function, together with associated income.

The City Council will account for its treasury management activities, for decisions made and transactions executed, in accordance with appropriate accounting practices and standards, and with statutory and regulatory requirements in force for the time being.

The City Council will ensure that its auditors, and those charged with regulatory review, have access to all information and papers supporting the activities of the treasury management function as are necessary for the proper fulfilment of their roles, and that such information and papers demonstrate compliance with external and internal policies and approved practices."

TMP8 **Cash and Cash Flow Management**

"Unless statutory or regulatory requirements demand otherwise, all monies in the hands of this organisation will be under the control of the responsible officer, and will be aggregated for cash flow and investment management purposes. Cash flow projections will be prepared on a regular and timely basis, and the Head of Finance will ensure that these are adequate for the purposes of monitoring compliance with TMP1[1] *liquidity risk management*."

TMP9 **Money Laundering**

"The City Council is alert to the possibility that it may become the subject of an attempt to involve it in a transaction involving the laundering of money. Accordingly, it will maintain procedures for verifying and recording the identity of counterparties and reporting suspicions, and will ensure that staff involved in this are properly trained.

TMP10 **Staff Training and Qualifications**

"The City Council recognises the importance of ensuring that all staff involved in the treasury management function are fully equipped to undertake the duties and responsibilities allocated to them. It will therefore seek to appoint individuals who are both capable and experienced and will provide training for staff to enable them to acquire and maintain an appropriate level of expertise, knowledge and skills. The Head of Finance will recommend and implement the necessary arrangements."

TMP11 **Use of External Service Providers**

"The City Council recognises the potential value of employing external providers of treasury management services, in order to acquire access to specialist skills and resources. When it employs such service providers, it will ensure it does so for reasons which will have been submitted to a full evaluation of the costs and benefits. It will also ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented, and subjected to regular review." Appendix C3 sets out the principal external service providers.

TMP12 **Corporate Governance**

"The City Council is committed to the pursuit of proper corporate governance throughout its businesses and services, and to establishing the principles and practices by which this can be achieved. Accordingly, the treasury management function and its activities will be undertaken with openness and transparency, honesty, integrity and accountability.

The City Council has adopted and has implemented the key recommendations of the Code. This, together with the other arrangements detailed in the schedule to this document, is considered vital to the achievement of proper corporate governance in treasury management, and the Head of Finance will monitor and, if and when necessary, report upon the effectiveness of these arrangements."

DEFINITION OF APPROVED ORGANISATIONS FOR INVESTMENTS

The following organisations constitute the counterparties with whom temporary investments will be made to the limits quoted:-

		<u>Cash</u> <u>Limit</u>	<u>Time</u> <u>Limit</u>
1.	<u>Public Sector</u>		
	Local Authorities in England:		
	- County Councils	£3m	364 days
	- Metropolitan, London Borough and Unitary Councils	£3m	364 days
	- District Councils	£2m	364 days
	Local Authorities in Scotland & Wales	£3m	364 days
	Local Authorities in Northern Ireland	£2m	364 days
	Public Corporations and Nationalised Industries		
	- United Kingdom	£3m	364 days
	No changes are proposed to the above limits.		
2.	<u>Building Societies</u>	<u>Cash</u> <u>Limit</u>	<u>Time</u> <u>Limit</u>
	Asset Base in excess of £1bn	£3m	364 days
	Asset Base £300m - £999m	£2m	364 days
	Asset Base £100m - £299m	£1m	6 months
	Asset Base below £100m	NIL	NIL
	No changes are proposed to the above limits.		
3.	<u>Clearing Bank Sector</u>	<u>Cash</u> <u>Limit</u>	<u>Time</u> <u>Limit</u>
		<u>Legal</u> <u>Rating</u> <u>(IBCA)</u>	
	*Abbey National plc	2	£3m 364 days
	- Abbey National Treasury Services		£3m 364 days
	- Cater Allan		£1m 364 days
	*Alliance & Leicester plc	2	£3m 364 days
	- Alliance & Leicester Group Treasury		£1m 364 days
	*Bank of Scotland	2	£3m 364 days
	- Bank of Scotland Treasury Services (HBOS)		£3m 364 days

*Barclays Bank plc	1		£3m	364 days
- Barclays de Zoete Wedd (BZW)			£1m	364 days
- Barclays Bank Trust Co Ltd			£1m	364 days
- Woolwich plc	3		£3m	364 days
Halifax plc	2		£3m	364 days
*HSBC plc	2	{	£3m	364 days
- HSBC Asset Finance		{	£1m	364 days
- (formerly Forward Trust Ltd)		{		364 days
*Lloyds/T.S.B. Group	2	{	£3m	364 days
- Cheltenham & Gloucester plc		{	£1m	364 days
- Hill Samuel Bank Ltd		{	£1m	364 days
- T.S.B.Scotland plc		{	£1m	364 days
- United Dominions Trust Ltd		{	£1m	364 days
*National Westminster Bank plc	1	{	£3m	364 days
- Coutts & Co		{	£1m	364 days
- Lombard Bank Ltd		{	£1m	364 days
- Lombard North Central plc		{	£1m	364 days
- Lombard & Ulster Ltd		{	£1m	364 days
- Ulster Bank Markets Ltd		{	£1m	364 days
- Ulster Bank Ltd		{	£1m	364 days
Northern Rock plc	4		£2m	364 days
*Royal Bank of Scotland	1	{	£3m	364 days
- Adam & Co plc		{	£1m	364 days
- Royscot Trust plc		{	£1m	364 days

* Total group investments not to exceed £3m at any one time.

No changes are proposed to the above limits apart from setting a £3m limit for each banking group as a further means of spreading any risk.

4. Merchant Banking Sector

No deposits are to be placed with the Merchant Bank Sector.

5. Foreign Banks

No investment deposits are to be placed with U K branches of Foreign Banks for the time being, with the exception of those funds held in connection with management of the City of Carlisle Investment Fund.

6. *Supranational Bodies

	Cash Limit	Time Limit
1. The European Atomic Energy Community.	}	
2. The European Coal and Steel Community.	}	

3.	The European Economic Community.	}		
4.	The European Investment Bank.	}		
5.	The International Bank for Reconstruction and Development.	}		
6.	The International Finance Corporation.	}	£15 million	5 Years
7.	The International Monetary Fund	}	maximum in	
8.	The African Development Bank.	}	total	
9.	The Asian Development Bank.	}		
10.	The Caribbean Development Bank.	}		
11.	The Inter-American Development Bank.	}		
12.	The Guaranteed Export Finance Corporation PLC.	}		
*	Subject to retaining their AAA credit rating	}		

No change is proposed to the above limits.

Fitch/IBCA Legal Ratings

Fitch/IBCA is the only rating agency, as far as is known, which publishes an explicit opinion on the likelihood of government support. In forming its credit ratings for banks, IBCA combines a "legal" rating with an "individual" rating. However, both the "legal" and "individual" ratings are published separately. The "legal" rating definition is as follows:

1. A clear legal guarantee exists or a high likelihood of forthcoming support from the state exists, given the importance of a bank.
2. Forthcoming support expected, even in the absence of a legal guarantee, given the importance of a bank.
3. Likely shareholder support, given the reputation and resources of the institutional owners.
4. Likely, but uncertain support.
5. Cannot rely on outside assistance.

In determining which banks shall be included within the list of approved counterparties, I feel that normally only banks with a legal rating of 1, 2 or 3 should be admitted. The Northern Rock has though been included on the list as although it converted to plc status in 1997 in many respects it is still a building society in terms of its assets and core business. However the lower lending limit is retained in view of the present rating.

DEFINITION OF APPROVED SOURCES OF FINANCING

The following list specifies those sources of finance which the City Council may adopt during 2003/04:

- Public Works Loans Board
- Stock Issue
- Money Market (Temporary and Long-Term)
- Local Temporary
- Overdraft
- Internal Capital Receipts and Revenue Balances
- Leasing – Financial and Operational

Finance will only be raised in accordance with the Local Government and Housing Act 1989. All forms of funding will be considered dependent upon the prevailing economic climate and other relevant factors.

EXTERNAL SERVICE PROVIDERS1. CITY OF CARLISLE INVESTMENT FUND

The City Council has appointed Morley Fund Management to manage surplus funds arising from 'frozen' set aside capital receipts via the City of Carlisle Investment Fund (the Fund). The current value of the Fund is £15m and is projected to rise to £15.6m during 2003/04. Morley Fund Management were appointed on a three year minimum period mandate with effect from 1 February 2003.

The City Council has previously satisfied itself as to the legality of these arrangements for external management. Documentation relating to the appointment of a fund manager covers:-

- terms of appointment;
- performance criteria and fee payment;
- objectives and limits;
- reporting;
- security and repayment;
- indemnity.

2. SECTOR TREASURY SERVICES

The City Council has appointed Sector Treasury Services as consultant advisers in connection with treasury management activities. The appointment is the subject of regular review.

EXTERNAL BORROWING DETERMINATIONS 2003/04

1. INTRODUCTION

1.1 Part IV of the 1989 Local Government and Housing Act introduced new controls on local authority borrowing, both on a day to day basis and on a longer term basis for funding capital expenditure. Before the start of each financial year, a local authority must now determine for the following year:

- i) An overall borrowing limit for that year.
- ii) A short term borrowing limit within that overall limit.
- iii) A limit on the proportion of the total interest payable by a local authority which can be varied by the lender or by reference to external factors.

1.2 These determinations must be made by a full meeting of the City Council and cannot be delegated to a Committee or an Officer of the Council. While these determinations can subsequently be varied during the year, again this can only be done by a full meeting of the City Council. However day to day administration of the agreed borrowings can be delegated to a Committee or an Officer and I would recommend that as at present this authority continue to be delegated to the City Treasurer or in his absence the Head of Financial Services.

2. DETERMINING THE BORROWING CEILING

2.1 In determining the overall borrowing limit the following items must be taken into account:

- 2.1.1 Monies required temporarily for revenue purposes. This is the shortfall in monies receivable but not received to the extent that they are required to meet revenue expenditure already disbursed together with any shortfall in income or deficit incurred on the previous year's account.

For the City Council the major source of income receivable comes from the collection of Council Tax and National Non-Domestic Rates which together total £61.5m. The largest single item of expenditure is to meet the County and Police Precepts which total £32.8m. I recommend that a figure of 20% of income receivable from the above sources be included in the calculation - i.e. £12.3m - together with the extent to which the Collection Fund may be in net deficit at 31st March 2003 and for which recovery action will continue. This sum is estimated at £1.0m.

- 2.1.2 Monies required temporarily for capital purposes. This includes capital expenditure incurred in the previous eighteen months which is due to be reimbursed out of grants but which has not yet been received together with capital expenditure incurred in the year of account to the extent that this is still to be financed by a longer term borrowing for which the City Council holds a valid credit approval.

For 2003/04 credit approvals for capital purposes total £1.3m and this figure should be included within the temporary borrowing limit.

- 2.1.3 The City Council's credit ceiling.
Following the LSVT, the City Council's credit ceiling is estimated at £10.1m.
- 2.1.4 The level of City Council approved investments and cash reserves.
All of the City Council's investments fall within the 'approved' definition and together with cash reserves are expected to total £40m at 31st March 2003.
- 2.1.5 The level of the City Council's usable capital receipts.
The balance of usable capital receipts available to finance capital expenditure and not applied at 31st March 2003 is expected to be £1m.
- 2.1.6 Amounts specified by the Secretary of State under directions.
In the main this will relate to local authorities with high levels of rent arrears for which an application can be made for a consent to borrow temporarily. It may also relate to arrears of Community Charge over three years old in excess of any provision maintained against non-collection. Neither factor applies to the City Council.

3. RECOMMENDATIONS

- 3.1 On the basis of the information set out in paragraph 2, I recommend that for 2003/04 the City Council be asked to resolve that:

- (i) The City Council's overall borrowing limit be set at £65.7m.
- (ii) Within the overall borrowing limit and subject to compliance with the detailed Regulations the short term borrowing limit be set at £14.6m.
- (iii) The limit on the proportion of loans taken up which are subject to variable interest rates, whether at the discretion of the lender or by reference to external factors be set at 100% in respect of short term loans, and also 100% in respect of long term loans taken up in 2003/04. This latter limit would be subject to the proportion of total City Council long term loans outstanding subject to variable interest rates not being in excess of 30%.

- (iv) The administration and control over all borrowings, the issue of loans instruments, and the making of all investments remain delegated to the Head of Finance, or in her absence the Strategic Finance and Business Analyst.

3.2 Members should be reassured that on a day to day basis the Regulations operate in such a way as to impose much lower limits on borrowings than are suggested in the above recommendations. These reflect a fall back position which would only come into question in the event of a significant failure in collection procedures.