



Decision No 2015/89

REPORT TO: Police and Crime Commissioner for Lancashire

REPORT BY: Steve Freeman, Chief Finance Officer

DATE: 29th March 2016

TITLE: **TREASURY MANAGEMENT POLICY AND STRATEGY 2016/17**

Appendix A refers

EXECUTIVE SUMMARY

This report outlines the proposed Treasury Management Policy Framework for 2016/17 as required by the Chartered Institute of Public Finance and Accountancy (CIPFA) Treasury Management Code of Practice (2011). It includes the Police and Crime Commissioner's borrowing and investment strategies, together with the treasury management prudential indicators which seek to ensure that the Commissioner's borrowing to fund capital expenditure remain both sustainable and affordable.

RECOMMENDATION

The Police and Crime Commissioner is recommended to:

- Approve the Treasury Management Strategy for 2016/17 and the Treasury Policy as set out at Appendix A.
- Approve the inclusion of the Municipal Bond Agency as an eligible counterparty for longer term capital funding.

Decision taken by the Police and Crime Commissioner for Lancashire:

Original decision, as set out in the attached report, approved without amendment (please delete as appropriate)	YES	NO

Original decision required to be amended and decision as detailed below:

The reasons for the amended decision are as detailed below:

Police and Crime Commissioner: Comments

DECLARATIONS OF INTEREST

The PCC is asked to consider any personal / prejudicial interests he may have to disclose in relation to the matter under consideration in accordance with the law, the Nolan Principles and the Code of Conduct.

STATEMENT OF COMPLIANCE

The recommendations are made further to legal advice from the Monitoring Officer and the Section 151 Officer has confirmed that they do not incur unlawful expenditure. They are also compliant with equality legislation.

Signed: 

Police and Crime Commissioner

Date: 29th March 2016

Signed: 

Chief Officer: 

Date: 29.3.2016

Signed:

Chief Constable

Date:

Signed: 

Chief Finance Officer:

Date: 29/3/16

Background

Treasury management is defined as “The management of the authority’s investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks.”

In February 2012 The Police and Crime Commissioner adopted the Chartered Institute of Public Finance and Accountancy’s Treasury Management in the Public Services: Code of Practice 2011 Edition (the CIPFA Code) which requires the approval of a treasury management strategy before the start of each financial year. As a local authority the Police and Crime Commissioner for Lancashire (“the Commissioner”) is also bound by the treasury management framework expressed within the code and therefore the requirements of the code must be met by Police and Crime Commissioners.

In addition, the Department for Communities and Local Government (CLG) issued revised guidance on local authority investments in March 2010 that requires Authorities, including Police and Crime Commissioners, to approve an investment strategy before the start of each financial year. The strategy also has regard to other CIPFA treasury management publications such as risk management in ‘Treasury Risk Toolkit for Local Authorities’ (2012) and the use of derivatives in ‘Using Financial Instruments to Manage Risk’ (2013.)

Statutory requirements

The Local Government Act 2003 (the Act) and supporting Regulations requires the Commissioner to “have regard to” the CIPFA Prudential Code and the CIPFA Treasury Management Code of Practice to set Prudential and Treasury Indicators for the next three years to ensure that the Commissioner’s capital investment plans are affordable, prudent and sustainable.

This report fulfils the Commissioner’s legal obligation under the *Local Government Act 2003* to have regard to both the CIPFA Code and the CLG Guidance.

CIPFA requirements

The primary requirements of the CIPFA Code are as follows-

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Commissioner’s treasury management activities, the current version is shown at Appendix 1.
2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Commissioner will seek to achieve those policies and objectives.
3. The production of an annual Treasury Management Strategy Statement - including the Annual Investment Strategy and Minimum Revenue Provision Policy - for the year ahead, a Mid-year Review Report and an Annual Report (stewardship report) covering activities during the previous year.
4. Delegation by the Commissioner of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

Treasury Management Strategy for 2016/17

This Strategy Statement has been prepared in accordance with the Code of Practice (2011). In accordance with the code, the Treasury Management Strategy will be approved by the Commissioner before the start of the financial year. In addition to this the Commissioner will also receive a mid-year report and a final year-end outturn report. In addition there will be monitoring and review reports provided in the event of any changes to Treasury Management policies or practices. The aim of these reporting arrangements is to ensure that those with ultimate responsibility for the treasury management function appreciate fully the implications of treasury management policies and activities, and that those implementing policies and executing transactions have properly fulfilled their responsibilities with regard to delegation and reporting.

The following reporting arrangements will be adopted in accordance with the requirements of the revised Code: -

Area of Responsibility	Committee/ Officer	Frequency
Treasury Management Policy Statement	Police and Crime Commissioner	Annually before the start of the financial year.
Treasury Management Strategy / Annual Investment Strategy / MRP policy – scrutiny and approval	Police and Crime Commissioner	Annually before the start of the financial year
Treasury Management Strategy / Annual Investment Strategy / MRP policy – midyear report, scrutiny of performance	Police and Crime Commissioner	Mid-year – 6 months
Treasury Management Strategy / Annual Investment Strategy / MRP policy – updates or revisions at other times	Police and Crime Commissioner	As required
Annual Treasury Management Outturn Report	Police and Crime Commissioner	Annually by 30 September
Treasury Management Monitoring Reports	Chief Finance Officer	Quarterly
Treasury Management Practices	Chief Finance Officer	Annually

In setting the Treasury Management Strategy, the following factors have been taken into account; economic forecasts, the level of the approved Capital Programme and the current structure of the Commissioner's debt portfolio. It covers the following aspects of the Treasury Management function:-

- Prudential Indicators which will provide a controlling framework for treasury management activities.
- Long-term debt outstanding;
- Prospects for interest rates;
- The Borrowing Strategy;
- The Investment Strategy;
- Policy on borrowing in advance of need.

Economic Context

The domestic economy has continued to grow with an estimated annual growth rate in 2015 of 2.2%. However there is considerable uncertainty in the economy arising from both the European Union Referendum and international economic position.

Much of the uncertainty is arising from the referendum on whether or not Britain should remain in the European Union. At this stage the impact of any decision on currency exchange rates, inflation, interest rates and future growth is subject to debate.

The global economy is facing a period of slower which will impact on UK growth and interest rates. China's growth has slowed and its economy is performing below expectations, reducing global demand for commodities and contributing to emerging market weakness. Although The US Federal Reserve increased interest rates by 0.25% in December the US economy is showing signs of slower growth and it is now anticipated that interest rates in the US in 2016 will not be a great as initially anticipated. The Eurozone is also suffering from low growth and inflation to the extent that there are negative interest rates in the attempt to stimulate growth.

Growth and inflation in 2016 are now expected to be lower than previously forecast. In the Chancellor of the Exchequer's Budget in March 2016 the growth figures were revised downwards from those provided in the Autumn Statement 2015 throughout the period covered by the budget. The GDP growth forecast are:

	2016/17	2017/18	2018/19	2019/20
	%	%	%	%
Budget 2016	2.0	2.2	2.1	2.1
Autumn Statement 2015	2.5	2.4	2.4	2.3

The forecast of the next expected increase in interest rates is now predicted to be as late as 2018.

Credit outlook

The varying fortunes of different parts of the global economy are reflected in market indicators of credit risk. UK Banks operating in the Far East and parts of mainland Europe have seen their perceived risk increase, while those with a more domestic focus continue to show improvement. The sale of most of the government's stake in Lloyds and the first sale of its shares in RBS have generally been seen as credit positive.

Current Treasury Portfolio Position

The current value of the Commissioner's Treasury Portfolio at 31.12.2015 is:	Principal £m	%
DEBT		
Fixed rate loans from PWLB	18.654	100
Variable rate loans	0	0
Total debt	18.654	
INVESTMENTS		
Variable rate investments in the County Council's General County Fund estimated for 31/3/2015 @ 0.5%	30.382	
3 yr Fixed Loan to UK local authority matures 23/10/17 @ 1.50%	5.000	
Senior Secured Bond Fund	5.000	
Total investments	40.382	

The level of investments represents the Commissioner's cumulative surplus on the General Fund, the balances on other cash-backed earmarked reserves and a cash-flow balance generated by a surplus of creditors over debtors and by grant receipts in advance of payments. There is net surplus position of £21.728m as at 31 December 2015 which is expected to fall to £17.728m at the end of the 2016/17 financial year.

Borrowing Requirement, Strategy and Prospects for Interest Rates.

The table below shows the total borrowing requirement for the current and the next three years.

The Commissioner has not borrowed for capital purposes since 2007, preferring instead to fund capital expenditure and maturing borrowing from internal resources.

	2015/16 Revised £m	2016/17 £m	2017/18 £m	2018/19 £m
Capital Programme Expenditure	17.569	30.962	27.390	10.360
<i>Financed by:</i>				
Capital Receipts	0.000	6.323	1.000	0.150
Grants and Contributions	2.756	1.499	1.293	1.293
Revenue Contributions	2.519	4.119	4.019	2.519
Capital & Transition Reserves	12.256	6.645	7.343	5.371
Borrowing	0.038	12.376	13.735	1.027
<i>Add Maturing Debt to be replaced:</i>				
Long Term PWLB	0.500	0.500	1.100	1.100
Previous Year Borrowing Requirement brought forward	0.000	5.000	5.000	7.868
Less Statutory Charge to Revenue	(1.292)	(1.257)	(1.237)	(1.276)
Total Borrowing Requirement	(0.754)	16.619	18.598	8.719

Capital Funding Strategy

The Commissioner has set aside funding in ear-marked revenue reserves to contribute to the delivery of the investment included in the Capital Programme. This resource will be used, in the first instance, to provide finance for short life assets such as IT systems and equipment in order to avoid the use of borrowing where possible for this type of asset. This approach represents a prudent strategy for the funding of short life assets as the cost of borrowing over shorter terms is more expensive than for longer periods and the use of reserves to minimise such shorter life borrowing represents better value for money.

Interest Rate Forecast and Prospects for Market Liquidity

The prevailing and forecast interest rate situation will be monitored to ensure that opportunities for debt restructuring are maximised. Regular forecasts of interest rates are provided by Arlingclose Ltd, treasury management advisers to Lancashire County Council.

Treasury Consultants Arlingclose Ltd forecast the first rise for official interest rates to be in the second quarter of 2018. It is expected that there will be a gradual pace of increases thereafter. Arlingclose are also forecasting that when the economy reaches the point that it can be considered to have recovered from the financial crisis, and rates rise to 'normal' levels, bank rate will range between 2.5% and 3.5%, considerably lower than pre-crisis levels.

The latest forecast provided by Arlingclose Ltd is shown in the table below:

	Bank Rate	3 Month LIBID	12 Month LIBID	5 Year Gilt Yield	10 Year Gilt Yield	20 Year Gilt Yield	50 Year Gilt Yield
Mar-16	0.50	0.60	1.00	0.93	1.50	2.30	2.35
Jun-16	0.50	0.60	1.00	0.95	1.65	2.35	2.40
Sep-16	0.50	0.60	1.05	1.00	1.70	2.40	2.30
Dec-16	0.50	0.65	1.10	1.05	1.75	2.50	2.55
Mar-17	0.50	0.65	1.10	1.10	1.80	2.60	2.65
Jun-17	0.50	0.70	1.15	1.20	1.90	2.65	2.68
Sep-17	0.50	0.70	1.20	1.30	2.00	2.65	2.70
Dec-17	0.50	0.75	1.25	1.40	2.05	2.65	2.75
Mar-18	0.50	0.80	1.30	1.50	2.10	2.70	2.75
Jun-18	0.50	0.85	1.35	1.55	2.15	2.75	2.75
Sep-18	0.75	0.85	1.35	1.60	2.20	2.75	2.80
Dec-18	0.75	0.90	1.40	1.65	2.25	2.80	2.85

In the above table 'bank rate' refers to the policy rate of the Bank of England. 'LIBID' is the London Interbank bid rate and can be used as a proxy for short term market interest rates. PWLB borrowing rates are based on 'Gilt Yield' and so this is a forecast of long term interest rates. The Commissioner can borrow at 80 basis points above the gilt yield, so for example a fixed interest rate to borrow PWLB money for 10 years would be 2.30%, 1.50% plus 0.80%.

This forecast has been based on the following underlying assumptions:-

- UK economic was resilient in 2015 with an estimated growth rate of 2.2%
- Household spending has been the main driver of GDP growth through 2014 and 2015 and remains key to growth. Consumption will continue to be supported by real wage and disposable income growth.
- Annual average earnings growth was 1.9% in the three months to December. Given low inflation, real earnings and income growth continue to run at relatively strong levels and could feed directly into unit labour costs and households' disposable income. Improving productivity growth should support pay growth in the medium term. The development of wage growth is one of the factors being closely monitored by the MPC.
- Business sentiment is being impacted by the uncertainty over the EU referendum and increasing uncertainties surrounding global growth and recent financial market shocks.
- Inflation is currently very low and, with a further fall in commodity prices, will likely remain so over the next 12 months. The CPI rate is likely to rise towards the end of 2016.
- China's growth has slowed and its economy is performing below expectations, which in turn will dampen activity in countries with which it has close economic ties; its slowdown and emerging market weakness will reduce demand for commodities. Other possible currency interventions following China's recent devaluation will keep sterling strong against many global currencies and depress imported inflation.
- US growth is showing signs of slowing but it is not expected it will slip into recession.

- Longer term rates will be tempered by international uncertainties and weaker global inflation pressure.

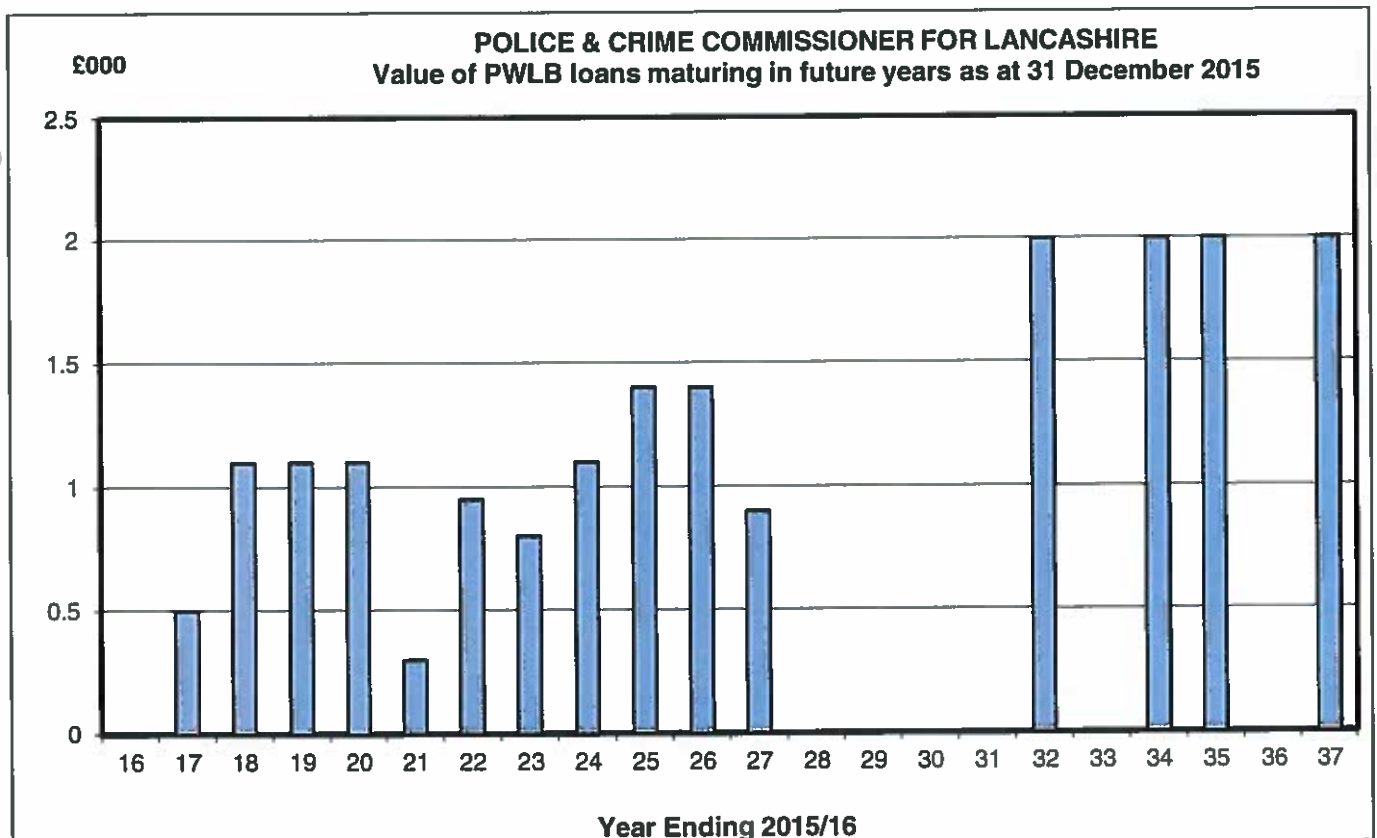
These factors will maintain the current direction of the MPC in the medium term.

Borrowing Strategy

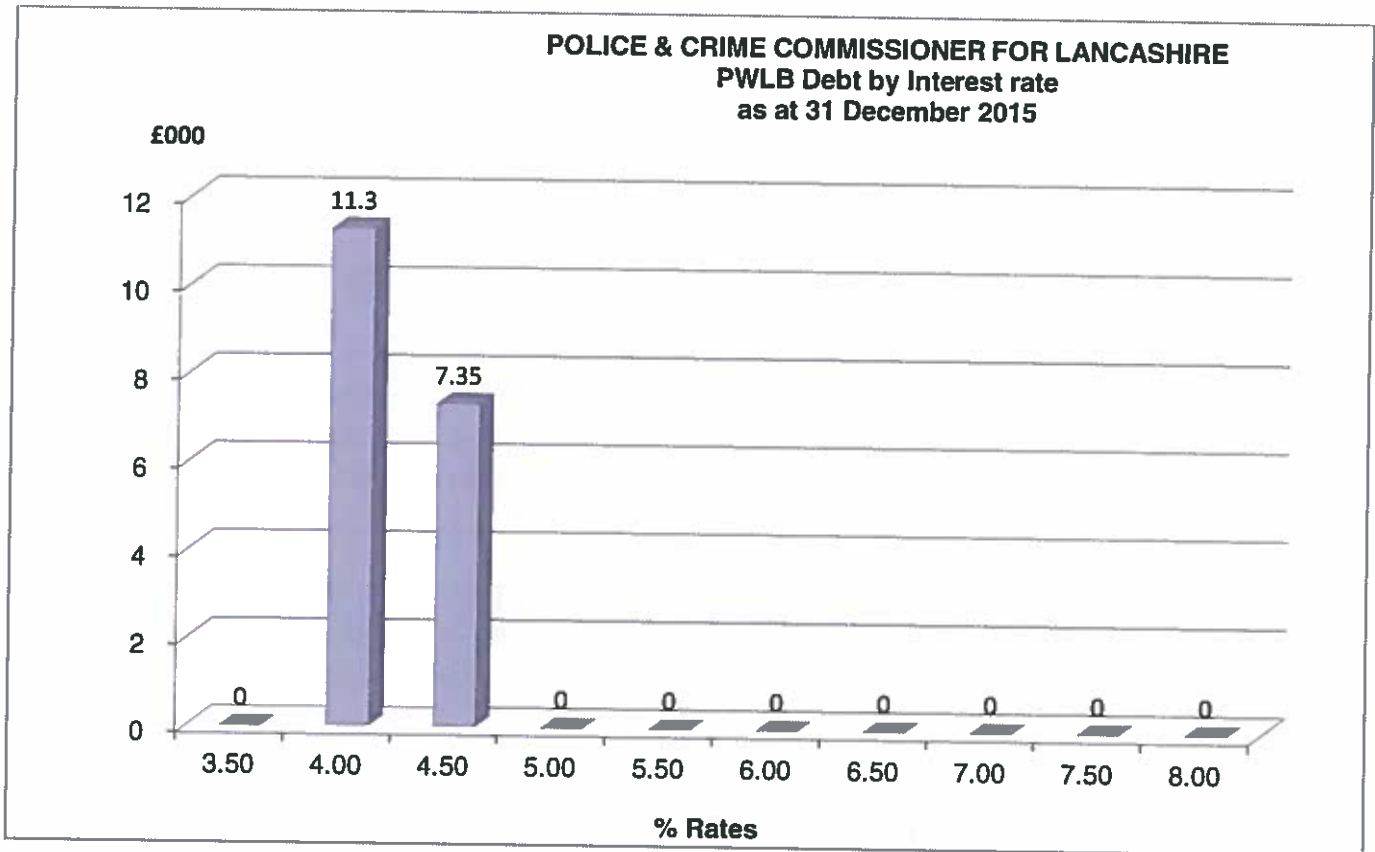
In view of the above interest rate forecast the Commissioner's borrowing strategy will be based upon the following information:-

- The UK remains in a gradually recovering but still relatively slow growth situation and with a tight fiscal and loose monetary policy approach it could be 2018 before official UK interest rates rise. Gilt yields are projected to be flat in the short term but on an upward path through the medium term.
- If it were felt that there was a significant risk of a sharp fall in long and short term rates, e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.
- If it were felt that there was a significant risk of a much sharper rise in long and short term rates than that currently forecast, perhaps arising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

The chart below shows the current maturity profile of the Commissioner's borrowings.



The chart below shows the same borrowings analysed by interest rate.



The cheapest borrowing at present is internal borrowing facilitated by running down cash balances and foregoing interest earned on investments at historically low rates - this is the policy the Commissioner has been pursuing for a number of years, funding capital expenditure and paying down debt maturities from existing balances. The immediate future is likely to see a continuation of this policy.

However, whilst such a strategy is most likely to be beneficial over the next 2-3 years as official interest rates remain low, it is unlikely to be sustained in the medium-term. The benefits of internal borrowing will be monitored regularly against the potential for incurring additional costs by deferring borrowing into future years when long-term borrowing rates are forecast to rise. In addition the Commissioner may borrow short term loans to cover unexpected cash flow shortages.

The approved sources of long-term and short-term borrowing currently are:

- Public Works Loan Board
- UK local authorities
- any institution approved for investments
- any other bank or building society authorised by the Prudential Regulation Authority to operate in the UK
- UK public and private sector pension funds

In the past the Commissioner has raised all long-term borrowing from the Public Works Loan Board, but it continues to investigate other sources of finance, such as local authority loans and bank loans, that may be available at more favourable rates.

GLA Municipal Bond Agency

The Municipal Bond Agency was established by the Local Government Association in June 2014 with the primary objective of setting up an alternative capital funding source for the local government sector and reducing UK local authority financing costs by becoming the most efficient and cost effective provider of finance. The company is owned by the LGA who are the founder shareholder and 56 other local authority shareholders one of which is Lancashire County Council.

It is expected that the MBA will make the first tranche of borrowing available to local authorities in 2016. In order to borrow from the MBA the each local authority is required to sign a joint and several guarantee contained within a framework agreement which is currently being considered by the County Council's legal department.

If following due diligence it is decided the Municipal Bond Agency is a suitable counterparty for borrowing, a separate report including information on the joint and several guarantee will be presented for consideration.

Debt Restructuring

The Chief Finance Officer, together with the County Council's treasury management team reviews options for debt restructuring on a regular basis. A recent review found that given the relatively favourable interest rates at which these have been taken out (below 5%) and the penalties associated with any early repayment, restructure is not considered financially viable at the present time. A better option for the immediate future is to utilise reserves to reduce the future borrowing requirement rather than repay debt.

Frequent discussions will continue to take place between the Chief Finance Officer and the Treasury Management Team to monitor this situation and any future decisions on debt financing will be put through the same rigorous cost and prudence analysis that external borrowing has traditionally gone through and will be reported to the Commissioner in due course.

Policy on Borrowing in Advance of Need

The Commissioner will not borrow more than or in advance of need purely in order to profit from the investment of the extra sums borrowed. However advance borrowing may be taken if it is considered that current rates are more favourable than future rates and that this advantage outweighs the cost of carrying advance borrowing. Any decision to borrow in advance will be considered carefully to ensure value for money can be demonstrated and that the Commissioner can ensure the security of such funds and relationships.

In determining whether borrowing will be undertaken in advance of need the Commissioner will:-

- Ensure that there is a clear link between the capital programme and the maturity profile of the existing debt portfolio which supports the need to take funding in advance of need.
- Ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered.
- Evaluate the economic and market factors that might influence the manner and timing of any decision to borrow.
- Consider the merits and demerits of alternative forms of funding.
- Consider the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.

Investment Strategy

The Commissioner will have regard to the CLG's Guidance on Local Government Investments ("the Guidance") issued in March 2004, any revisions to that guidance, the Audit Commission's report on Icelandic investments and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Guidance Notes ("the CIPFA TM Code"). The Commissioner's investment priorities are: -

- (a) The security of capital and
- (b) The liquidity of its investments.

The Commissioner will also aim to achieve the optimum return on his investments commensurate with proper levels of security and liquidity. The risk appetite of the Commissioner is low in order to give priority to security of its investments and in accordance with this the 2015/16 policy needs to take into account the recent developments in banking reform legislation.

Current Investments

At 31st December 2015 the Commissioner held £40.43m invested funds, representing income received in advance of expenditure plus balances and reserves held. In the past 12 months, the Commissioner's investment balance has ranged between £84.65m and £16.54m, and similar levels are expected to be maintained in the forthcoming year.

In line with the 2015-16 treasury management strategy which continues the policy of credit risk reduction following the financial crisis, the Commissioner will only use very high quality counterparties for investments. All of the Commissioner's investments are currently with other local authorities

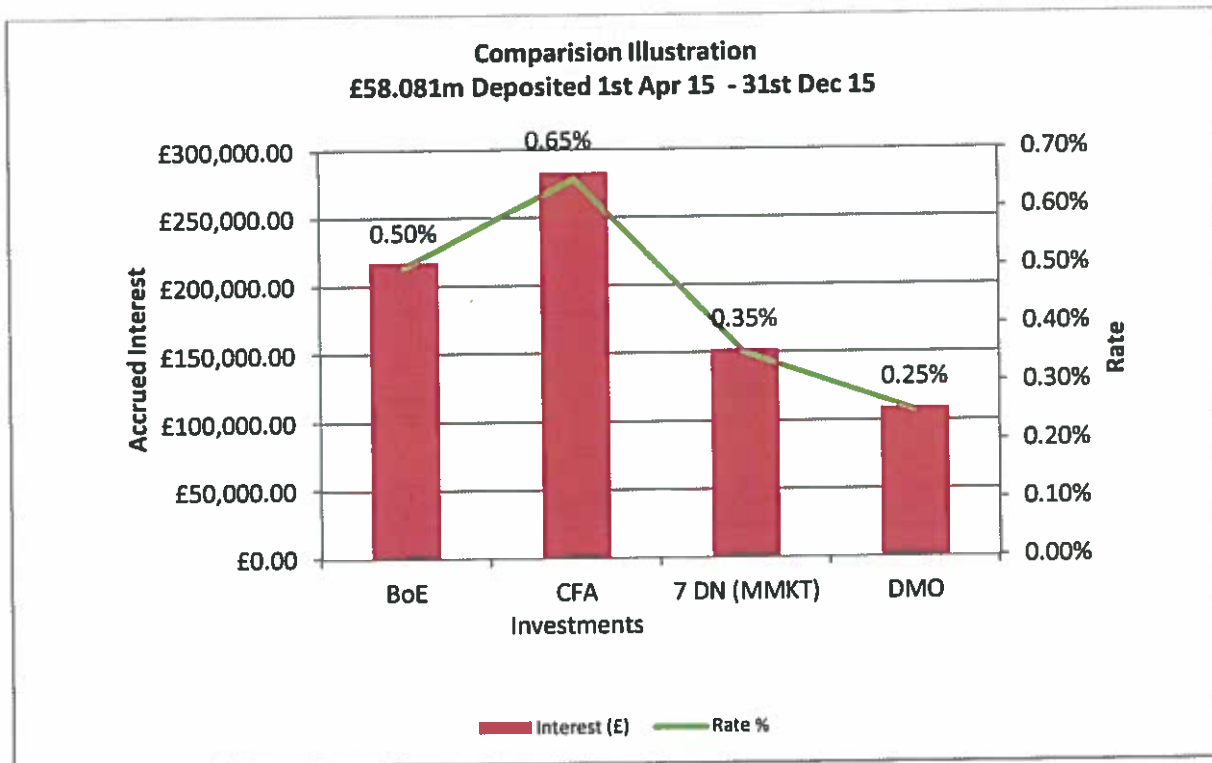
The Commissioner currently has access to a call (instant access) account, which currently pays bank rate, this is currently 0.50%. Each working day the balance on the Commissioner's Current Account is invested in this to ensure that the interest received on surplus balances is maximised.

Secondary liquidity is provided through the AAA rated 24 Asset Management Senior Secured Bond Fund. A £5m investment was made in this fund in July 2015. The cash is callable with 3 days' notice, and is currently yielding 0.62%

In addition a long term loan has been placed with another UK local authority as outlined below:

Start Date	End Date	Principal	Rate	Annual Interest	Interest 2015/16
22/10/14	23/10/17	£5,000,000	1.5%	£75,000	£75,000

The overall combined amount of interest earned on Fixed/Call balances as at 31st December 2015 is £256k on an average balance of £58.081m at an annualised rate of 0.65%. The current interest rate is 0.69%. This compares favourably with the benchmark 7 day LIBID which averages 0.36% over the same period, and is 0.15% above bank rate and 0.40% above the UK Government debt management office rate. These margins are illustrated in the chart below:



The low interest rate environment is also illustrated in the graph below which shows the UK Government (Gilt) yield curve on 26/02/16 showing the rate of return on gilts for various maturities. For example the return on a gilt maturing two years from now is 0.3248% and for a 5 year investment the rate is 0.6915%.



Both the CIPFA Code and the CLG Guidance require the Commissioner to invest its funds prudently, and to have regard to the security and liquidity of its investments before seeking the highest rate of return, or yield. The Commissioner's objective when investing money is to strike

an appropriate balance between risk and return, minimising the risk of incurring losses from defaults and the risk of receiving unsuitably low investment income.

The Commissioner may invest surplus funds with any of the counterparties in the table below, subject to the cash and time limits shown.

Counterparty		Cash limit	Time limit †
Secured Bank Deposits, Reverse repurchase Agreements	AAA	£5m each	5 years*
	AA+		3 years*
	AA		2 years*
	AA-		2 years*
Call Accounts with banks and other organisations with minimum AA- credit rating		£10m	next day
UK Central Government (irrespective of credit rating)		unlimited	50 years**
UK Local Authorities (irrespective of credit rating)		unlimited	50 years**
Secured Bond Funds AA rating and WAL not more than 3 yrs		£5m each	n/a
Secured Bond Funds AAA rated and WAL not more than 5 yrs		£5m each	n/a

* but no longer than 2 years in fixed-term deposits and other illiquid instruments

** but no longer than 5 years in fixed-term deposits and other illiquid instruments

Legislative Context

Bail-in legislation, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers in the future, has now been fully implemented in the UK, USA and Germany. The rest of the European Union will follow suit in January 2016, while Australia, Canada and Switzerland are well advanced with their own plans. Meanwhile, changes to the UK Financial Services Compensation Scheme and similar European schemes in July 2015 mean that most private sector investors are now partially or fully exempt from contributing to a bail-in. The current policy reflects this legislation in that unsecured bank deposits and money market funds have also been removed from the 16/17 policy because they are subject to the new bank bail-in legislation and other regulatory uncertainties.

In the 15/16 policy a replacement liquidity option through bond funds was included within the treasury policy with allowable funds defined by credit rating and weighted average life (WAL.) Investing in senior secured bonds backed by collateral provides a protection against bail-in.

For 2016/17 it is recommended that secured lending is extended to include repurchase agreements.

Whilst the investment strategy has been amended to allow greater flexibility with investments any decision as to whether to utilise this facility will be made based on an assessment of risk and reward undertaken jointly between the Chief Finance Officer and LCC Treasury Management Team, and consideration of this forms part of the on-going meetings that take place throughout the year.

The legislative and regulatory background to treasury management activities requires the Commissioner to set out the use of “specified” and “non-specified” investments.

Specified Investments: The CLG Guidance defines specified investments as those:-

- denominated in pound sterling,
- due to be repaid within 12 months of arrangement,
- not defined as capital expenditure by legislation, and invested with one of:
 - the UK Government,
 - a UK local authority, parish council or community council, or
 - a body or investment scheme of “high credit quality”.

The Commissioner defines “high credit quality” organisations as those having a credit rating of A+ or higher that are domiciled in the UK or a foreign country with a sovereign rating of AA+ or higher.

○ Non-Specified Investments are any investment that does not meet the definition of a specified investment. The Commissioner does not intend to make any investments denominated in foreign currencies, nor any that are defined as capital expenditure by legislation, such as company shares. Non-specified investments will therefore be limited to long-term investments, i.e. those that are due to mature 12 months or longer from the date of arrangement, and investments with bodies and schemes not meeting the definition of specified credit quality.

The Commissioner may lend or invest money using any of the following instruments:-

- interest-bearing bank accounts,
- fixed term deposits and loans,
- callable deposits where the Commissioner may demand repayment at any time (with or without notice),
- certificates of deposit,
- bonds, notes, bills, commercial paper and other marketable instruments, and
- shares in bond funds

○ Investments may be made at either a fixed rate of interest, or at a variable rate linked to a market interest rate, such as LIBOR, subject to the limits on interest rate exposures below.

On behalf of the Commissioner the county council's treasury management section prepares daily cash flow forecasts to determine the maximum period for which funds may prudently be committed. The forecast is compiled on a pessimistic basis, with receipts under-estimated and payments over-estimated to minimise the risk of being forced to borrow on unfavourable terms to meet its financial commitments. Limits on long-term investments are set by reference to the Commissioner's medium term financial plan and cash flow forecast.

The performance target on investments will remain as being above the average rate for 7 day notice money.

7. Minimum Revenue Provision (MRP) Strategy

The previous Lancashire Police Authority implemented the new Minimum Revenue Provision (MRP) guidance in 2008/09 and this was subsequently adopted by the Commissioner. The Commissioner is required to assess MRP for 2016/17 in accordance with the main

recommendations contained within the guidance issued by the Secretary of State under section 21(1A) of the Local Government Act 2003.

The major proportion of the MRP will relate to the more historic debt liability that will continue to be charged at the rate of 4%, in accordance with the Capital Financing Requirement method for MRP calculation. This option allows for the MRP to be calculated as 4% of the Capital Financing Requirement. The CFR is derived from the Balance Sheet and represent the value of the fixed assets, for which financing provision has not already been made. This method of calculation has been used by the Authority since the introduction of the MRP in 2004. Unsupported borrowing reflected within the debt liability at 31st March 2010 will under delegated powers be subject to MRP under the Asset life method, which will be charged over a period which is reasonably commensurate with the estimated useful life applicable to the nature of expenditure, using the equal annual instalment method. For example, capital expenditure on a new building, or on the refurbishment or enhancement of a building, will be related to the estimated life of that building.

Estimated life periods will be determined under delegated powers. To the extent that expenditure is not on the creation of an asset and is of a type that is subject to estimated life periods that are referred to in the guidance, these periods will generally be adopted by the Commissioner. However, the Commissioner reserves the right to determine useful life periods and prudent MRP in exceptional circumstances where the recommendations of the guidance would not be appropriate.

As some types of capital expenditure incurred by the Commissioner are not capable of being related to an individual asset, asset lives will be assessed on a basis which most reasonably reflects the anticipated period of benefit that arises from the expenditure. Also, whatever type of expenditure is involved, it will be grouped together in a manner which reflects the nature of the main component of expenditure and will only be divided up in cases where there are two or more major components with substantially different useful economic lives.

In summary it is proposed that the Commissioner continues to use the Capital Financing Requirement option as applied to all supported borrowing.

The Commissioner currently applies the Asset Life method (Equal Charge approach) to capital expenditure financed by unsupported borrowing and it is proposed that this option also be continued.

The capital programme contains a scheme for the replacement of Blackpool police station which will involve an additional MRP charge to cover the financing of the new asset. This charge will be deferred, using current capital financing regulations, until the asset becomes fully operational, when savings will be realised from the restructure of the existing facilities.

Prudential Indicators for 2016/17 to 2018/19 in respect of the Police and Crime Commissioner's Treasury Management Activities.

In accordance with its statutory duty and with the requirements of the Prudential Code for Capital Finance and the CIPFA Code for Treasury Management, every local authority produces each year a set of prudential indicators which regulate and control its treasury management activities.

The following table sets out the debt and investment-related indicators which provide the framework for the Commissioner's proposed borrowing and lending activities over the coming three years. These indicators will also be approved by members as part of the Capital Programme

approval process along with other capital expenditure-related indicators, but need to be reaffirmed and approved as part of this Treasury Management Strategy.

Treasury Management Prudential Indicators	2015/16 (Revised) £000	2016/17 £000	2017/18 £000	2018/19 £000
1. Adoption of the Revised CIPFA Code of Practice on Treasury Management	Adopted for all years in January 2012			
2. Authorised limit for external debt - A prudent estimate of external debt, which includes sufficient headroom for unusual cash movements.				
Borrowing	23,000	39,000	56,000	63,000
Other long-term liabilities	1,000	1,000	1,000	1,000
TOTAL	24,000	40,000	57,000	64,000
3. Operational boundary for external debt - A prudent estimate of debt, but no provision for unusual cash movements. It represents the estimated maximum external debt arising as a consequence of the Commissioner's current plans.				
Borrowing	20,000	36,000	53,000	60,000
Other long-term liabilities	1,000	1,000	1,000	1,000
TOTAL	21,000	37,000	54,000	61,000

4. Gross Debt / Capital Financing Requirement Indicator

	<u>2015/16 (Rev)</u> £m	<u>2016/17</u> £m	<u>2017/18</u> £m	<u>2018/19</u> £m
Capital Financing Requirement	35.552	46.635	59.113	58.904
Maximum Gross Debt	17.400	33.518	51.017	58.454
Debt to CFR	48.9%	71.9%	86.3%	99.2%

This is a measure of prudence recently introduced into the code. The fact that gross debt is less than the capital financing requirement is taken as an indicator borrowing has only been made for capital purposes.

5. Upper limit for fixed interest rate exposure

Upper limit of borrowing at fixed rates	100%	100%	100%	100%
Upper limit of investments at fixed rates	100%	100%	100%	100%

6. Upper limit for variable rate exposure

Upper limit of borrowing at variable rates	75%	75%	75%	75%
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Upper limit of investments at variable rates	100%	100%	100%	100%
7. Upper limit for total principal sums invested for over 364 days (per maturity date as a percentage of total investments.)	75%	75%	75%	75%
8. Maturity structure of Debt	Upper Limit		Lower Limit	
	%		%	
Under 12 months	50		-	
12 months and within 24 months	50		-	
24 months and within 5 years	50		-	
5 years and within 10 years	80		-	
10 years and above	90		25	
	<u>2015/16</u>	<u>2016/17</u>	<u>2017/18</u>	<u>2018/19</u>
	<u>(Rev)</u>			
9. <u>Ratio of financing costs to revenue stream</u>	0.77%	0.84%	1.06%	1.07%
10. <u>Estimate of impact of capital investment on council tax</u>		£26.24	£28.41	£20.70
11. <u>Estimate of impact of capital investment on council tax NET of revenue contributions to capital</u>		£0.47	£1.48	£2.18

Decision Required

The Commissioner is asked to approve the treasury management strategy for 2016/17, including

- a) Treasury management prudential indicators
- b) The borrowing strategy
- c) The investment strategy
- d) The MRP strategy
- e) To formally adopt the updated policy statement at Appendix A

Treasury Management Policy Statement

The Police and Crime Commissioner's financial regulations require him to create and maintain a treasury management policy statement, stating the policies, objectives and approach to risk management of his treasury activities, as a cornerstone for effective treasury management.

Definition

The Police and Crime Commissioner defines his treasury management activities as: the management of the Commissioner's investments and cash flows, his 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.

Risk management

The Commissioner regards the successful identification, monitoring and control of risk to be the prime criteria by which the effectiveness of his treasury management activities will be measured. Accordingly, the analysis and reporting of treasury management activities will focus on their risk implications for the organisation, and any financial instruments entered into to manage these risks.

Value for money

The Commissioner acknowledges that effective treasury management will provide support towards the achievement of its business and service objectives. He is therefore committed to the principles of achieving value for money in treasury management, and to employing suitable comprehensive performance measurement techniques, within the context of effective risk management.

Borrowing policy

The Commissioner greatly values revenue budget stability and will therefore borrow the majority of its long-term funding needs at long-term fixed rates of interest. However, short-term and variable rate loans may be borrowed to either offset short-term and variable rate investments or to produce revenue savings. The Commissioner will also constantly evaluate debt restructuring opportunities of the existing portfolio,

The Commissioner will set an affordable borrowing limit each year in compliance with the *Local Government Act 2003*, and will have regard to the *CIPFA Prudential Code for Capital Finance in Local Authorities* when setting that limit. He will also set limits on its exposure to changes in interest rates and limits on the maturity structure of its borrowing in the treasury management strategy report each year.

Investment policy

The Commissioner's primary objectives for the investment of his surplus funds are to protect the principal sums invested from loss, and to ensure adequate liquidity so that funds are available for expenditure when needed. The generation of investment income to support the provision of services is an important, but secondary, objective.

The Commissioner will have regard to the *Communities and Local Government Guidance on Local Government Investments* and will approve an investment strategy each year as part of the treasury management strategy. The strategy will set criteria to determine suitable organisations with which cash may be invested, limits on the maximum duration of such investments and limits on the amount of cash that may be invested with any one organisation.

