Report of	Meeting	Date
Director of Transformation	Audit Committee	30 June 2010

Treasury Management Annual Report 2009/10

PURPOSE OF REPORT

This report, prepared in accordance with the CIPFA Prudential Code for Capital Finance in Local Authorities, summarises the treasury activities of the Council for 2009/10, and gives updated information on recovery of Icelandic investments.

RECOMMENDATION(S)

That the Audit Committee:

1. Note and comment as appropriate on the content of the report and appendices.
2. Note the treasury position and performance against prudential indicators for 2009/10 as set out in the report.
3. Note the charging of the £510,309 impairment, net of interest, for Icelandic Investments to the 2009/10 General Fund Accounts.

EXECUTIVE SUMMARY OF REPORT

The report confirms compliance with key prudential indicators, that compliance with the investment benchmark was achieved, and reports the current legal opinion that the priority creditor status of Local Authorities pursuing recovery of Icelandic investments remains the most likely outcome despite legal challenge by other creditors.

REASONS FOR RECOMMENDATION(S)
(If the recommendations are accepted)

1. It is a statutory requirement that Councils receive an annual report on treasury matters following the end of the year.

ALTERNATIVE OPTIONS CONSIDERED AND REJECTED

2. None

CORPORATE PRIORITIES

3. This report relates to the following Strategic Objectives:

Put Chorley at the heart of regional economic development in the Central Lancashire sub-region		Develop local solutions to climate change.	
Improving equality of opportunity and life chances		Develop the Character and feel of Chorley as a good place to live	
Involving people in their communities		Ensure Chorley Borough Council is a performing organization	X

BACKGROUND

The Chartered Institute of Public Finance and Accountancy's (CIPFA) Code of Practice on Treasury Management 2009 has been adopted by the Council and this Council fully complies with its requirements.

The primary requirements of the Code are as follows:

1. Creation and maintenance of a Treasury Management Policy Statement which sets out the policies and objectives of the Council's treasury management activities.

2. Creation and maintenance of Treasury Management Practices which set out the manner in which the Council will seek to achieve those policies and objectives.

3. Receipt by the Full Council of an annual treasury management strategy (including the annual investment strategy*)* for the year ahead, a midyear review (as a minimum) and an annual review at the end of the year.

4. Delegation by the Council of responsibilities for implementing and monitoring treasury management policies and practices and for the execution and administration of treasury management decisions.

5. Delegation by the Council of the role of scrutiny of treasury management strategy and policies to a specific named body which in this Council is the Audit Committee.

Treasury management in this context is defined as:

"The management of the local authority's investments and cash flows, its banking, money market and capital market transactions; the effective control of the risks associated with those activities; and the pursuit of optimum performance consistent with those risks. "

The purpose of this report is to meet one of the above requirements of the CIPFA Code, namely the annual review of treasury management activities, for the financial year 2009/10.

Reports previously submitted

In March 2009 Council approved the Treasury Strategy 2009/10 to 2011/12, the Investment Strategy 2009/10 and the related Treasury Prudential Indicators. In summary, these satisfy best practice and regulatory requirements relating to treasury operations providing:

- Details of expected treasury activities of the Council for the year acting as a base position against which performance can be monitored and reported upon;
- The rules and boundaries within which the Council will operate with regard to treasury activities.

Reports reviewing performance and compliance, and advising on progress with the Icelandic investment, were submitted on 13 August 2009 and 11 November 2009.

DETAIL
TREASURY POSITION at 31 MARCH 2010

The treasury position at the 31st March 2010 compared with the previous year was:

	Principal		
	31st March 2009 **£m**	**31st March 2010** **£m**	**Movement in 2009/10** **£m**
Long term (over 1 year) borrowing	2.280	0.900	(1.380)
Short term borrowing	2.389	1.380	(1.009)
Temporary borrowing	0	1.400	1.400
Total Debt (all fixed rate)	**4.669**	**3.680**	**(0.989)**
Short term fixed interest investments	5.009	1.896	(3.113)

The investments total includes Landbanki at its impaired value of £1.489m at 31 March 2010.

The authority's approved Treasury and Investment Strategies in 2009/10 and 2010/11 have taken full account of the continued turbulence in financial markets and have been informed by support and advice from the Council's specialist treasury advisors. The strategies:

- Placed strong restrictions on the financial institutions (counterparties) in which the Council has been able to make investments.
- Recognised that the low Bank of England Base Rate would impact on investment returns and that this is likely to continue for some time.

There were no changes in the Bank of England Base Rate during 2009/10. The last change took place on 5th March 2009 when the rate fell to 0.5%.

LANDSBANKI

Efforts to secure recovery of the Councils frozen deposits in Landsbanki (£2m) are ongoing. In this we work through the Local Government Association (LGA) whose specialist legal advisors are working collectively on behalf of all local authorities with deposits in Icelandic banks. The latest position is as follows:

- The Council's claim has been accepted by the Winding Up Board as having priority status. This position has been challenged by the unsecured creditors of Landsbanki but the LGA's specialist legal advisors opinion is that "it remains the most likely outcome that the claims will enjoy priority status".
- Agreement has now been reached on the terms of the deal that will compensate creditors of "old" Landsbanki (including local authorities) in relation to assets transferred to "new" Landsbanki (which was set up to ensure the maintenance of a banking system in Iceland following the collapse of the old banks).
- As anticipated, the "forecast" recovery rate continues to fluctuate as time moves on and better information becomes available. The latest forecast suggests that recoveries will amount to 95% of claims but that repayments will be made over a significantly longer time, to October 2018. It also advises that penalty rates of interest will not be claimable for the period between the due redemption date and the claim date (22 April 2009). The combined effect of these changes is to necessitate an increase of £189k in the impairment. This has been charged to the 2009/10 accounts.

Understanding the figures concerning Landsbanki, as they appear in the Statement of Accounts and in this report, is difficult. The following table is therefore given to provide a comprehensive picture:

		£
Principal originally invested		2,000,000
2008/9 Interest (deferred to 2009/10)	165,189	
2008/9 Impairment (deferred to 2009/10)	(569,826)	(404,637)
Book value at 31/3/09		1,595,363
2009/10 Interest accruing	83,888	
2009/10 Further impairment	(189,560)	(105,672)
Book value at 31/3/10		1,489,691

The methodology used is prescribed for authorities by CIPFA. Its key features are as follows

1. The Council's claim is for principal and interest up to 22 April 2009. Originally this totalled £2.192m inclusive of penalty interest. Penalty interest has now been dropped lowering the claim to £2.072m.
2. Recovery of 95% will realise £1.965m. Since receipts will be phased until 2018 they are "discounted" to reflect the loss of interest. Crucially we have to assume a discount rate of 5.81%, the original coupon, even though it does not reflect current earning power. This reduces the "value" of the receipts to a "present value" of £1.406m.
3. The "impairment" reported in the accounts and elsewhere, of £0.759m. is the difference between the value at 31 March 2009, £2.165m, and the "present value" £1.406m.
4. The high discount rate has had the effect of increasing the impairment charge which has hit Chorley's accounts in 2009/10. However the "flip" side of this is that in future years we will continue to accrue interest on the outstanding investment at 5.81%, far in excess of current interest rates.
5. The 2008/9 impairment and interest transactions were deferred until 2009/10. In the current year therefore the net charge of £510,309 (as above) has been made.

BORROWINGS

The Council's borrowings are subject to half yearly repayments of principal and this resulted in the repayment of £2.389m over the course of 2009/10. It was anticipated that by year end the Council's liquid balances would be eliminated, and this proved to be the case resulting in temporary borrowing of £1.4m over the period 26 March to 1 April 2010.

Post year end activity

Since the year end cash receipts have followed the usual pattern for this time of year in exceeding outgoings, and cash balances have risen to a healthy level. This is however only a temporary feature and the basic cash shortage, resulting from the repayment of our borrowings, and the demands of the capital programme, will evidence itself as the year progresses. The 2010/11 treasury strategy envisaged borrowing during the year of up to £8.5m and the target interest rate, identified in discussions with the Council's advisor Sector Treasury Consultants, was 2.5% for a 5 year loan. As a result of the Greek debt crisis, and the related Euro problems, interest rates dipped markedly, and £5m was borrowed at 2.4% on 25 May 2010.

INVESTMENTS

The following table summarises investment activity during 2009/10.

Details	Average daily investment £'000	Interest earned £	Average Rate
Money Market Funds	975	5,566	0.57%
Short term deposits	1,353	6,871	0.51%
Call accounts	2,616	22,530	0.86%
Debt Management Office (DMO)	2,356	6,397	0.27%
Total – Short term	**7,300**	**41,364**	**0.57%**

<u>Short term Investments</u>

The Council's Investment Strategy is extremely cautious, restricting counterparties to only the highest rated British institutions or those owned or supported by the Government. This has made use of the Debt Management Office, despite it offering a very low rate, unavoidable.

The benchmark against which the investment performance is judged is the 7 day London Interbank Rate (LIBID).This represents a minimum level of return on cash invested for a minimum period. The average 7 day LIBID rate for 2009/10 was 0.421%. The actual return, as shown above, was 0.57%.

TREASURY ADVISORS

Treasury services to the Council are now provided within the Financial Shared Services Arrangement with South Ribble Borough Council. During the latter part of 2009/10 the two Councils undertook a procurement exercise and appointed Sector Treasury Services as a single external advisor to both Councils for the period 1st April 2010 to 31st March 2013. This brings the benefit of improved service and economies of scale.

PRUDENTIAL INDICATORS AND COMPLIANCE ISSUES

The Local Government Act 2003 requires the Council to adopt the CIPFA Prudential Code and produce prudential indicators. These are set at the start of the year and provide targets for expected activity and establish boundaries and limits upon that activity. **<u>Appendix A</u>** summarises performance during the year against each of these indicators for 2009/10.

The only significant differences between the planned and out-turn positions concern capital expenditure and, the Capital Financing Requirement.

Capital expenditure has increased by £0.6m. The only large addition is the cost of capitalising of statutory redundancy (£0.29m). All changes have been reported during the year.

The Capital Financing Requirement (CFR) is a measure of the Council's underlying need to borrow money or take out leases to fund its capital programme. Its importance is that it has to be "paid off" and thus any increase has budget implications. The increase shown in appendix A, of £0.8m. is largely the result of the increase in capital expenditure coupled with changes in some of the assumed capital resources.

The prudential code requires that net borrowing should not exceed the CFR. In Chorley net borrowing (i.e. borrowing less investments, is £1.784m at 31 March 2010, comfortably less than the CFR of £9.674m.

IMPLICATIONS OF REPORT

4. This report affects the following areas. The relevant Directors' comments are attached:

Finance	X	Customer Services	
Human Resources		Equality and Diversity	
Legal	X	No significant implications in this area	

COMMENTS OF THE STATUTORY FINANCE OFFICER

5. This report meets statutory requirements. Its statistical content is consistent with the Councils financial accounts for the year 2009/10

DIRECTOR NAME Gary Hall
DIRECTOR DESIGNATION Statutory Finance Officer

Document	Inspection
Financial Strategy/Budget and Council Tax 2010/11 Treasury Management in the Public Services: Code of Practice CIPFA Prudential Code for Capital Finance in Local Authorities Treasury Management Report to Governance Committee 22/9/09	Town Hall***

Report Author	Ext	Date	Doc ID
G Whitehead***	515485	18/06/10	***

Appendix A

Treasury Management Prudential Indicators

Estimated and Actual Treasury Position and Prudential Indicators

		2009/10 Actual £'000	2009/10 Estimate £'000
1	**Capital Expenditure**	5,668	5,053
2	**Capital financing Requirement at 31 March**	9,674	8,882
3	**Authorised Limit for external debt** **- for comparison maximum actual debt**	 4683	10,892
4	**Operational Boundary for external debt** **- for comparison maximum external debt**	 4,683	8,892
3	**Ratio of financing costs to net revenue stream**	0.63%	0.76%
4	**Incremental impact of capital investment decisions on the Band D Council Tax**	n/a	-£0.32
5	**Upper limits on fixed interest rates based on net debt**	100%	100%
6	**Upper limits on variable interest rates based on net debt**	Nil	30%
7	**Maturity structure of fixed interest rate borrowing (against maximum position)**		Lower & upper limits
	Under 12 months	75%	0% to 100%
	12 months to 2 years	20%	0% to 100%
	2 years to 5 years	5%	0% to 100%
	5 years to 10 years	0	0% to 25%
	10 years and above	0%	0% to 25%
8	**Maximum principal funds invested for periods longer than 364 days (against maximum position)**	0	0

In addition to the above the Council is required as a prudential indicator to:

- Adopt the CIPFA Code of Practice

The compliance with these indicators is highlighted in the body of the report.