ARDS AND NORTH DOWN BOROUGH COUNCIL

4 February 2020

Dear Sir/Madam

You are hereby invited to attend a Special Council Meeting which will be held in the **Council Chamber, Town Hall, The Castle, Bangor** on **Tuesday, 11 February 2020** commencing at **7.00 pm.**

Tea, coffee and sandwiches will be available from 6.00pm.

Yours faithfully

Stephen Reid
Chief Executive
Ards and North Down Borough Council

A G E N D A

1. Prayer

2. Apologies

3. Declarations of Interest

*****IN CONFIDENCE*****

4. (i) Report of Special Corporate Services Committee dated 30 January 2020 (Copy attached)
   (ii) Report of Special Corporate Services Committee dated 6 February 2020 (Copy attached)

*****OUT OF CONFIDENCE*****

5. Prudential Codes (Report attached)

6. Robustness of Estimates and Adequacy of Reserves (Report attached)

7. District Rates 2020/21 (Report to be tabled)

MEMBERSHIP OF ARDS AND NORTH DOWN BOROUGH COUNCIL

Alderman Carson	Councillor S Dunlop
Alderman Gibson	Councillor Dunne
Alderman Girvan	Councillor Edmund
Alderman Irvine	Councillor Egan
Alderman Keery **(MAYOR)**	Councillor Gilmour
Alderman McDowell	Councillor Greer
Alderman McIlveen	Councillor Kennedy
Alderman Menagh	Councillor Mathison
Alderman Smith	Councillor Martin
Councillor Adair	Councillor McClean
Councillor Armstrong-Cotter	Councillor McKee
Councillor Blaney	Councillor McKimm
Councillor Boyle	Councillor McNickle
Councillor Brooks	Councillor McRandal
Councillor Cathcart	Councillor Smart
Councillor Chambers	Councillor P Smith
Councillor Cooper	Councillor T Smith
Councillor Cummings	Councillor Thompson
Councillor Douglas **(DEPUTY MAYOR)**	Councillor Walker
Councillor McAlpine	Councillor Wilson

ITEM 5

Ards and North Down Borough Council

Report Classification	Unclassified
Council/Committee	Council
Date of Meeting	11 February 2020
Responsible Director	Director of Finance and Performance
Responsible Head of Service	Head of Finance
Date of Report	07 February 2020
File Reference	FIN142
Legislation	Regulation 7 Local Government (Capital Finance and Accounting) Regulations (NI) 2011
Section 75 Compliant	Yes ☐ No ☐ Other ☒ If other, please add comment below:
Subject	Prudential Code Reports
Attachments	Appendices 1 Capital Strategy 2 Treasury Management Strategy

Capital Strategy

The Local Government Finance Act (NI) 2011 requires the Council to have regard to the Chartered Institute of Public Finance and Accountancy's (CIPFA) Prudential Code for Capital Finance in Local Authorities 2018 Edition (the Prudential Code) when determining how much money it can afford to borrow. The objectives of the Prudential Code are to ensure, within a clear framework, that the capital investment plans of local authorities are affordable, prudent and sustainable, and that treasury management decisions are taken in accordance with good professional practice.

This capital strategy is a new report for 2020/21, giving a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of Council services along with an overview of how associated risk is managed and the implications for future financial sustainability.

To demonstrate that the Council has fulfilled its objectives, the Capital Strategy sets out the indicators that must be set and monitored each year.

This strategy is set out in appendix 1 and the Prudential Code requires that it is made available on the Council website.

Treasury Management Strategy Statement

The Council is also required to adopt the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code), which requires the Council to approve a treasury management strategy before the start of each financial year.

In addition, the former Department of the Environment (DOE) issued Guidance on Local Council Investments in October 2011 that requires the Council to approve an investment strategy before the start of each financial year.

Appendix 2 fulfils the Council's legal obligation under the Local Government Finance Act (NI) 2011 to have regard to both the CIPFA Code and the DOE Guidance.

RECOMMENDATION

It is recommended that Council approves the Capital Strategy and Treasury Management Strategy Statement for 2020/21 financial year as set out in Appendices 1 and 2.

Capital Strategy Report 2020/21

Introduction

This capital strategy report gives a high-level overview of how capital expenditure, capital financing and treasury management activity contribute to the provision of Council services along with an overview of how associated risk is managed and the implications for future financial sustainability.

Decisions made this year on capital and treasury management will have financial consequences for many years into the future. They are therefore subject to both a national regulatory framework and to local policy framework, summarised in this report.

From 1 April 2020, due to a change in accounting rules, the Council will be required to bring onto its Balance Sheet any ‘right of use’ assets which it currently accounts for as operating leases. Operating leases are currently treated as ‘pay as you go’ arrangements, with rentals expensed (charged to the General Fund) in the year they are paid. In recognising any rights acquired under such leases to use an asset, the new rules now require that these assets are included on the Balance Sheet with a corresponding liability to repay the lease over its term. This has resulted in changes to the prudential indicators for 2020/21 and subsequent years, summarised where relevant in this report.

Capital Expenditure and Financing

Capital expenditure is where the Council spends money on assets, such as property or vehicles, that will be used for more than one year. In local government this may include spending on assets owned by other bodies. The Council has some limited discretion on what counts as capital expenditure, for example assets costing below £5,000 are not capitalised and are instead charged to revenue. In addition, expenditure incurred on enhancing an existing asset can be capitalised if it either extends the asset’s useful life or significantly enhances the service potential of the asset.

In 2020/21, the Council is planning capital expenditure of £7.529m as summarised below:

Table 1: Prudential Indicator: Estimates of Capital Expenditure in £ millions

Capital Expenditure by Directorate	2019/20 Forecast £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
Community & Wellbeing	1.035	2.102	5.797	9.176
Environment	1.892	1.648	1.600	1.800
Regeneration, Development & Planning	0.918	3.779	6.525	15.000
Other	0.025	-	-	0.150
Total Capital Expenditure	**3.870**	**7.529**	**13.922**	**26.126**
Add Leases onto Balance Sheet	-	4.668	-	-
Total Capital Expenditure (including Leases)	**3.870**	**12.197**	**13.922**	**26.126**

Capital expenditure to be incurred in 2020/21 includes the completion of new play and leisure facilities being provided with Peace IV Shared Spaces funding, regeneration works and improvements in the Borough's villages funded from the NI Rural Development Programme, the commencement of the Bangor Waterfront project with funding from the Belfast City Region Deal and the commencement of Portaferry Public Realm Scheme (also subject to central government funding). Other smaller schemes at Cairnwood and Donaghadee Motte will progress, together with new and upgraded playparks provision and replacement vehicles, plant and equipment.

Capital expenditure for 2020/21 also includes £4.668m due to the change in the accounting rules for leases.

Governance:

Each year as part of the Estimates process for the next financial year Council approves a capital investment plan, which allocates funding for capital projects for financial planning purposes.

In order to increase budgetary discipline and improve financial resilience, in October 2019 the Council agreed guiding principles within which to frame its financial plans. Four of these principles relate to capital expenditure and are:

- Minimum revenue provision holidays will not exceed the increase in underlying capital financing expenditure;
- Capital financing expenditure capped as a % of net income stream;

- The increase in capital financing expenditure capped at 1% of district rate rise; and
- Capital expenditure above funding caps not to be funded by borrowings.

In addition, all major schemes (ie. one-off projects with gross whole-life costs of greater than £500,000) have been ranked using a formal matrix based on corporate alignment, need, risk, readiness and cost-benefit score. This ranking will be reviewed at least once a year.

Projects with a whole life cost of less than £500,000 are not yet formally ranked. In addition, property maintenance and vehicle replacement strategies provide a framework within which this capital expenditure is incurred.

Projects cannot proceed until there has been some form of assessment of need. For one-off projects this takes the form of a business case or economic appraisal. For expenditure incurred as a result of a strategy, this assessment is in the form of condition surveys or other relevant forms of appraisal.

In addition, major capital schemes are overseen by individual project boards and a Corporate Projects Portfolio Board, which reports to the Council's Corporate Services Committee.

All capital expenditure must be financed, either from external sources (government grants and other contributions), the Council's own resources (revenue, reserves and capital receipts) or debt (borrowing and leasing). The planned financing of the above expenditure is as follows:

Table 2: Capital financing in £ millions

	2019/20 Forecast £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
Capital Grants & Contributions	1.147	3.273	7.169	14.988
Capital Receipts	0.874	1.340	0.155	0.100
Revenue	0.020	-	-	-
Debt (Borrowing)	1.829	2.916	6.598	11.038
Debt (Leases)	-	4.668	-	-
Total Financing	**3.870**	**12.197**	**13.922**	**26.126**

Debt is only a temporary source of finance, since loans and leases must be repaid, and this is therefore replaced over time by other financing, usually from revenue which is known as minimum revenue provision (MRP). The forecasts for MRP, which now include, due to the change in accounting rules, a provision for leases, are as follows:

Table 3: Replacement of debt finance in £ millions

	2019/20 Forecast £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
MRP	3.536	4.718	5.769	6.201

- The Council is required to approve an MRP statement each year. The full MRP statement for 2020/21 can be found on page 9 of this report.

The Council's cumulative outstanding amount of debt finance is measured by the capital financing requirement (CFR). This increases with new debt-financed capital expenditure and reduces with MRP. The CFR is expected to increase by £2.866m during 2020/21. Based on the above figures for expenditure and financing, the Council's estimated CFR is as follows:

Table 4: Prudential Indicator: Estimates of Capital Financing Requirement in £ millions

Capital Financing Requirement (CFR)	31.03.20 Forecast £m	31.03.21 Estimate £m	31.03.22 Estimate £m	31.03.23 Estimate £m
Opening CFR	**88.373**	**86.666**	**89.532**	**90.362**
Capital Expenditure	3.870	7.529	13.922	26.126
Leases onto Balance Sheet	-	4.668	-	-
Less Capital Grants	(1.147)	(3.273)	(7.168)	(14.988)
Less Capital Receipts applied	(0.874)	(1.340)	(0.155)	(0.100)
Less Reserves Financing	(0.020)	-	-	-
Less MRP (Borrowing)	(3.536)	(4.444)	(5.503)	(5.942)
Less MRP (Leases)	-	(0.274)	(0.266)	(0.259)
Total CFR	**86.666**	**89.532**	**90.362**	**95.199**

The capital financing requirement for 2020/21 and subsequent year includes a £4.668m increase due to the change in accounting rules for leases.

Asset management

To ensure that capital assets continue to be of long-term use, the Council recently approved an estates strategy and an estates management plan.

The strategy has three overarching objectives:

- To support a refreshed focus on communities and people, economic regeneration and tourism, the quality of our environment and the core services provided by the Council and is partners.
- To generate capital and revenue efficiencies to support the delivery of corporate objectives and improved social outcomes.
- To create linkage between capital receipts and revenue efficiencies and the process of developing and prioritising capital investment programmes.

It has been designed to align with the spirit of the *Big Plan* 'Creating Positive Outcomes for Everyone' – the Community Plan for Ards and North Down and to support the Council's new Corporate Plan which will be launched in April 2020.

On this basis the Estate Strategy will run until 2025 at which point in time it will be refreshed and updated to align with a new Corporate Plan.

Asset disposals

When a capital asset is no longer needed, it may be sold so that the proceeds, known as capital receipts, can be spent on new assets. The Council has included capital receipts of £207k in its financial plan as follows:

Table 5: Capital receipts in £ millions

	2019/20 Forecast £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
Asset sales	0.082	0.125	nil	nil

Treasury Management

Treasury management is concerned with keeping sufficient but not excessive cash available to meet the Council's spending needs, while managing the risks involved. Surplus cash is invested until required, while a shortage of cash will be met by borrowing, to avoid excessive credit balances or unauthorised overdrafts in the bank current account. The Council is typically cash rich in the short-term as revenue income is received before it is spent, but cash poor in the long-term as capital expenditure is incurred before being financed. The revenue cash surpluses are offset against capital cash shortfalls to reduce overall borrowing.

Due to decisions taken in the past, the Council currently has £74.2m long-term borrowing at an average interest rate of 5.9%, £7m short-term borrowings at an average rate of 0.96% and £8m short-term treasury investments at an average rate of 0.73%.

Borrowing strategy

The Council's main objectives, when borrowing, are to achieve a low but certain cost of finance, while retaining flexibility should plans change in future. These objectives are often conflicting, and the Council therefore seeks to strike a balance between cheap short-term loans (currently available at around 1%) and long-term fixed rate loans where the future cost is known but higher (currently up to 3.2%).

Projected levels of the Council's total outstanding debt (borrowings and leases) are shown below, compared with the capital financing requirement (see above).

Table 6: Prudential Indicator: Gross Debt and the Capital Financing Requirement in £ millions

	31.03.20 Forecast £m	31.03.21 Estimate £m	31.03.22 Estimate £m	31.03.23 Estimate £m
External Debt – Borrowing	81.244	82.253	83.402	88.282
External Debt - Leases	-	4.394	4.128	3.869
Total External Debt	81.244	86.647	87.53	92.151
Capital Financing Requirement	86.666	89.532	90.362	95.199
Internal Borrowing	**5.422**	**2.885**	**2.831**	**3.048**

Statutory guidance is that debt should remain below the capital financing requirement, except in the short-term. As can be seen from table 6, the Council expects to comply with this in the medium term.

The difference between the external debt and the capital financing requirement represents the Council's internal borrowing ie. the amount of cash backed reserves the Council has available to defer the need to externally borrow for capital purposes.

Affordable borrowing limit

The Council is legally obliged to set an affordable borrowing limit (also termed the authorised limit for external debt) each year. In line with statutory guidance, a lower "operational boundary" is also set as a warning level should debt approach the limit.

Table 7: Prudential Indicators: Authorised limit and operational boundary for external debt in £m

	2019/20 limit £m	2020/21 limit £m	2021/22 limit £m	2022/23 limit £m
Authorised limit – borrowing	89.717	90.138	91.234	96.330
Authorised limit – leases		5.894	5.628	5.369
Authorised limit – total external debt	89.717	96.032	96.862	101.699
Operational boundary – borrowing	81.422	85.138	86.234	91.330
Operational boundary – leases		4.894	4.628	4.369
Operational boundary – total external debt	81.422	90.032	90.862	95.699

The authorised limit and operational boundary for 2020/21 and subsequent years include an increase due to the change in the accounting for leases.

Treasury Investment strategy

Treasury investments arise from receiving cash before it is paid out again.

The Council's policy on treasury investments is to prioritise security and liquidity over yield, that is to focus on minimising risk rather than maximising returns. Cash that is likely to be spent in the near term is invested securely, for example with the government, other local authorities or selected high-quality banks, to minimise the risk of loss. Short-term investments may be held in pooled funds, where an external fund manager makes decisions on which particular investments to buy and the Council may request its money back at short notice. Further details on treasury investments are in in the treasury management strategy.

Governance

Decisions on treasury management investment and borrowing are made daily and are therefore delegated to the Director of Finance and Performance and staff, who must act in line with the treasury management strategy approved annually by Council. Reports on treasury management activity are presented to the Corporate Services Committee both during the year and the end of each financial year.

Liabilities

In addition to the forecast debt of £81.2m detailed above, the Council is committed to making future payments to cover its pension fund deficit valued at £35.6m (March 2019). It has also set aside £0.5m to cover risks of public and employee liability insurance claims and other environmental and legal liabilities. The Council is also at risk of having to pay a share of potential financial penalties associated with the procurement process of a residual waste treatment project. Council has not put aside any money for this purpose.

Governance

Decisions on incurring new discretional liabilities are taken by members of the Corporate Leadership Team in consultation with the Director of Finance and Performance. The risk of liabilities crystallising and requiring payment is monitored by individual directors and reported to the appropriate standing committee as necessary.

Revenue Budget Implications

Although capital expenditure is not charged directly to the revenue budget, interest payable on loans and MRP are charged to revenue, offset by any investment income receivable. The net annual charge is known as financing costs; this is compared to the net revenue stream i.e. the amount funded from District Rates and general government grants.

Table 9: Prudential Indicator: Proportion of financing costs to net revenue stream

	2019/20 Forecast £m	2020/21 Estimate £m	2021/22 Estimate £m	2022/23 Estimate £m
Financing costs (£m)	6.568	7.761	8.871	9.377
Proportion of net revenue stream	12.9%	13.8%	15.2%	15.6%

Financing costs for 2020/21 and subsequent years includes a total increase of £844k due to a change in the accounting rules for leases.

Sustainability

Due to the very long-term nature of capital expenditure and financing, the revenue budget implications of expenditure incurred in the next few years will extend for up to 40 years into the future. Due to the significant capital investment programme, Council has prioritised major capital expenditure with a view to ensuring that the proposed capital programme is prudent, affordable and sustainable in the longer term.

Knowledge and Skills

The Council employs professionally qualified and experienced staff in senior positions with responsibility for making capital expenditure, borrowing and investment decisions. For example, the Director of Finance and Performance, along with his senior Finance team, are qualified accountants with substantial experience. In addition, the Strategic Capital Development is led by a well experienced qualified architect. The Council pays for junior staff to study towards relevant professional qualifications.

Where Council staff do not have the knowledge and skills required, use is made of external advisers and consultants that are specialists in their field. The Council currently employs Arlingclose Limited as treasury management advisers and the Strategic Investment Board Ltd as property consultants. This approach is more cost effective than employing such staff directly and ensures that the Council has access to knowledge and skills commensurate with its risk appetite.

Annual Minimum Revenue Provision Policy Statement 2020/21

Where the Council finances capital expenditure by borrowings, it must put aside resources to repay that debt in later years. The amount charged to the revenue budget for the repayment of debt is known as Minimum Revenue Provision (MRP). The Act and the Local Government (Capital Finance and Accounting) Regulations (NI) 2011 require the Council to have regard to the Department of Environment's Guidance on Minimum Revenue Provision (the DOE Guidance), most recently issued in 2011.

The aim of the DOE Guidance is to ensure that debt is repaid over a period that is reasonably commensurate with the period over which the capital expenditure provides benefits. It requires the Council to approve an Annual MRP Statement each year.

From 1 April 2020, due to a change in accounting rules for leases, MRP will include prudent provision for future lease obligations. It is therefore recommended that Council approves the following MRP Statement for 2020/21:

- For capital expenditure incurred before 1st April 2012 and fully financed from borrowings, the revenue provision will be the sum of loan principal repayments due and amounts set aside for maturity loans on all borrowings taken out before 1st April 2012 ie. before the introduction of MRP.
- For capital expenditure incurred after 1st April 2012, MRP will be determined by charging the expenditure over the expected useful life of the relevant assets, in equal instalments, starting in the year after the asset becomes operational.
- MRP on expenditure not related to fixed assets, but which has been capitalised by regulation or direction (eg. public realm schemes), will be charged over the period in which the expenditure provides benefit.
- MRP for 'right of use' assets acquired by leases will be equal to the element of the rent or charge that goes to write down the balance sheet liability.
- Additional and holiday provisions in the form of voluntary revenue provision (VRP) may also be applied.

Based on the Council's forecast of its Capital Financing Requirement, the forecasts for MRP are as follows:

MRP Estimates	2019/20 £m	2020/21 £m	2021/22 £m	2022/23 £m
MRP on Capital Exp before 1 April 2012	2.124	2.109	2.061	2.021
MRP on Capital Exp after 1 April 2012	2.734	2.954	3.226	3.695
MRP not related to Capital Exp	0.216	0.216	0.216	0.226
MRP on leases from 01 April 2020	-	0.274	0.266	0.259
VRP	(1.538)	(0.835)	-	-
Total MRP	**3.536**	**4.718**	**5.769**	**6.201**

Treasury Management Strategy Statement 2020/21

Introduction

Treasury management is the management of the Council's cash flows, borrowing and investments, and the associated risks. The Council, when borrowing and/or investing substantial sums of money is exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. The successful identification, monitoring and control of financial risk are therefore central to the Council's prudent financial management.

Treasury risk management at the Council is conducted within the framework of the Chartered Institute of Public Finance and Accountancy's Treasury Management in the Public Services: Code of Practice 2017 Edition (the CIPFA Code) which requires the Council to approve a treasury management strategy before the start of each financial year. In addition, the former Department of the Environment (DoE) issued Guidance on Local Authority Investments in October 2011 that requires the Council to approve an investment strategy before the start of each financial year. This report fulfils the Authority's legal obligation under the Local Government Finance Act (Northern Ireland) 2011 to have regard to both the CIPFA Code and the DoE Guidance.

In accordance with the DOE Guidance, the Council will be asked to approve a revised Treasury Management Strategy Statement should the assumptions on which this report is based change significantly. Such circumstances would include, for example, a large unexpected change in interest rates, or in the Council's capital programme or in the level of its investment balance.

External Context

Economic background

The major external influence on the Council's treasury management strategy for 2020/21, as in the previous year, will be the UK's progress in future trading arrangements following its exit from the European Union and other geo-political factors.

Annual GDP growth for the domestic economy continues to remain below trend, currently at 1%. Looking ahead, the Bank of England's Monetary Policy Report (formerly the Inflation Report) forecasts economic growth to reach 2.1% by the end of 2022, with expectations for the economy to pick up during 2020 as Brexit-related uncertainties dissipate and provide a boost to business investment.

Credit outlook

Credit conditions for larger UK banks have remained relatively benign over the past year. However, with bail-in legislation now in place, which ensures that large investors including local authorities will rescue failing banks instead of taxpayers, Council has other investment options available to it with lower credit risk than unsecured bank deposits; returns from cash deposits will however also remain very low.

Interest rate forecast

The Council's treasury management adviser Arlingclose is forecasting that the Bank Rate will remain at 0.75% until the end of 2022. The risks to this forecast are deemed to be significantly weighted to the downside. The Bank of England, having previously indicated that interest rates may need to rise if a Brexit agreement was reached, now believe that this is less likely.

Gilt yields and hence long-term borrowing rates have risen but remain at low levels and only some very upward movement from current levels is expected based on Arlingclose's interest rate projections. Arlingclose projects that the 10-year and 20-year gilt yields will rise to around 1.0% and 1.4% respectively over the time horizon, with broadly balanced risks to both the upside and the downside. However short-term volatility arising from both economic and political events over the period is a near certainty.

Local Context

On 1 February 2020, the Council held £81.2m of borrowing and £8.0m of investments. The level of borrowings is not expected to change for the remaining months of the 2019/20 financial year, but the investment levels are expected to fall to around £2.0m.

Forecast changes in the capital financing and borrowing requirements over the next three financial years are shown in table 1 below.

Table 1: Balance Sheet Summary and Forecast

	31.3.19 Actual £m	31.3.20 Forecast £m	31.3.21 Estimate £m	31.3.22 Estimate £m	31.3.23 Estimate £m
Capital Financing Requirement	**88.3**	**86.6**	**89.5**	**90.3**	**95.2**
Less: External debt *	(78.9)	(81.2)	(86.6)	(87.5)	(92.2)
Internal borrowing	**9.4**	**5.4**	**2.9**	**2.8**	**3.0**

* from 01/04/20, external borrowing includes lease liabilities of £4.6m being brought onto the balance sheet due to a change in accounting rules.

The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The Council has an increasing CFR due to the capital investment programme but minimal investments, and will therefore be required to borrow up to £8.7m over the forecast period from April 2020 to March 2023.

CIPFA's Prudential Code for Capital Finance in Local Authorities recommends that the Council's total debt should be lower than its highest forecast CFR over the next three years. Table 1 above shows that the Council expects to comply with this recommendation during 2019/20.

Borrowing Strategy

The Council is forecast to hold £81.2m of total borrowings by 31 March 2020, an increase of £2.3m on the previous year, reflecting the Council's strategy for funding the capital programme after the utilisation of capital receipts and other usable reserves. The balance sheet forecast in table 1 above indicates only a modest increase in borrowing levels (excludes lease liabilities) of £0.8m by 31 March 2021. This is reflective of the Council's strategy to address the key issue of affordability resulting in limited capital expenditure in 2020/21 in line with its guiding principles on limiting the increase in capital financing expenditure to one percentage point of the district rate increase and funding capital expenditure above funding caps from sources other than borrowing.

Objectives

The Council's primary objective when borrowing money is to strike an appropriately low risk balance between securing low interest costs and achieving cost certainty over the period for which funds are required.

Strategy

With short-term interest rates currently much lower than long-term rates, it is likely to be more cost effective in the short-term to either use internal resources, or to borrow short-term loans instead.

Additionally, borrowing rates through the Public Works Loan Board (PWLB) are now around 2% higher than gilt yields, following an increase in these rates by 1% due to a change in government policy in October 2019.

The Council will likely therefore adopt a short-term borrowing approach for the coming year. The benefits of short-term borrowing ie. lower interest costs 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 modestly.

The Council will continue to monitor interest rates and seek advice from Arlingclose throughout the year. If interest rate forecasts change significantly, this may result in borrowing long-term at fixed rates in 2020/21 with a view to keeping future interest costs low, even if this causes additional cost in the short-term.

Approved Sources

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

- Government Loans Fund (via the Department of Finance, DoF);
- any institution approved for investments including UK local authorities, Government departments and arms-length bodies;
- any other bank or building society authorised to operate in the UK;
- UK public and private sector pension funds (except NILGOSC and NICS Pension Funds);
- capital market bond investors;
- UK Municipal Bonds Agency plc and other special purpose companies created to enable Council bond issues.

In addition, capital finance may be raised by the following methods that are not borrowing, but may be classed as other debt liabilities:

- leases;
- hire purchase;
- sale and leaseback.

The majority of the Council's long-term borrowing is from the Department of Finance but Officers will continue to investigate other sources of finance, such as local Council loans and bank loans, that may be available at more favourable rates. Discussions are continuing with the Department of Communities to determine if Northern Ireland Councils can access the more favourable rates, already accessible by Councils in Great Britain, from the Public Works Loan Board (PWLB). It is anticipated that most of the short-term borrowing will come from other UK local authorities.

LOBOs

The Council holds £2m of LOBO (Lender's Option Borrower's Option) loans where the lender has the option to propose an increase in the interest rate at set dates, following which the Council has the option to either accept the new rate or to repay the loan at no additional cost. Although lenders are unlikely to exercise their options in the current low interest rate environment, there remains an element of refinancing risk. The Council will take the option to repay LOBO loans at no cost if it is viable and it has the opportunity to do so. Below is a summary of the LOBO loans currently held by Council:

Lender	Loan Amount	Interest Rate	Expiry Date
Dresdner Bank AG	£1,000,000	5.500%	Sept 2023
Lloyds Bank	£1,000,000	6.590%	Apr 2025

Short-term and Variable Rate loans

These loans leave the Council exposed to the risk of short-term interest rate rises and are therefore subject to the limit on the net exposure to variable interest rates in the treasury management indicators below.

Debt Rescheduling

The Department of Finance allows Councils to repay loans before maturity and either pay a premium or receive a discount according to a set formula based on current interest rates. Other lenders may also be prepared to negotiate premature redemption terms. The Council may take advantage of this and replace some loans with new loans, or repay loans without replacement, where this is expected to lead to an overall cost saving or a reduction in risk.

Policy on Borrowing in advance of need

The Council will not borrow more than or in advance of its needs purely in order to speculate from the investment of the extra sums borrowed. However, the Council will consider borrowing in advance of its needs to hedge against future interest rate rises, although such a strategy will be discussed with the Council's advisors to ensure that the 'cost to carry' (the cost incurred when borrowing rates are higher than low risk investment rates) is carefully considered. Any decision to borrow in advance will also be within the forward approved Capital Financing Requirement estimates. Since amounts borrowed will be invested until spent, the Council is aware that it will be exposed to the risk of loss of the borrowed sums, and the risk that investment and borrowing interest rates may change in the intervening period. These risks will be managed as part of the Council's overall management of its treasury risks.

Investment Strategy

The Council currently holds invested funds of £8m, representing income received in advance of expenditure plus balances and reserves held. This level is expected to fall to £2m by the end of March 2020 and remain low during the 2020/21 year, as these funds are utilised to contribute to the financing of the capital investment programme.

Objectives

Both the CIPFA Code and the DOE Guidance require the Council 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 Council'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 receiving unsuitably low investment income.

Negative Interest Rates

If the UK enters into a recession in 2020/21, there is a small chance that the Bank of England could set its Bank Rate at or below zero, which is likely to feed through to negative interest rates on all low risk, short-term investment options. This situation already exists in many other European countries. In this event, security will be measured as receiving the contractually agreed amount at maturity, even though this may be less than the amount originally invested.

Strategy

The aim of the strategy is to generate a list of highly creditworthy counterparties which will enable diversification and thus avoidance of concentration risk. Most of the Council's surplus cash is invested in short-term unsecured bank deposits and money market funds. Given the increasing risk and continued low returns from short-term unsecured bank investments, the Council will aim to further diversify into more secure and higher yielding asset classes during 2020/21, if investment levels require it. Other than short-term investments of any monies borrowed in advance of need but within the authorised limits over the forecast period, it is expected however that only minimum levels of investments will be maintained.

Approved Counterparties

In accordance with guidance from the DOE and CIPFA and in order to minimise the risk to investments, the Council will only consider counterparties with a minimum acceptable credit quality for inclusion on the lending list. The Council will therefore adhere to the approved counterparty list provided by its treasury advisors, Arlingclose. Arlingclose consider credit ratings from a selection of exernal rating agencies together with other market factors, with the end product being a listing of the relative creditworthiness of counterparties. This information will be used by the Council to determine which counterparties to place investments with and the maximum duration for investments. Arlingclose will alert the Council to changes in counterparty creditworthiness and provide updated approved counterparty lists as these changes are notified. Where an entity has its credit rating downgraded so that it fails to meet the approved investment criteria then:

- no new investments will be made;
- any existing investments that can be recalled or sold at no cost will be; and
- full consideration will be given to the recall or sale of all other existing investments with the affected counterparty.

Where a credit rating agency announces that a credit rating is on review for possible downgrade (also known as "rating watch negative" or "credit watch negative") so that it may fall below the approved rating criteria, then only investments that can be withdrawn will be made with that organisation until the outcome of the review is announced. This policy will not apply to negative outlooks, which indicate a long-term direction of travel rather than an imminent change of rating.

Specified Investments

The Council deals only in specified investments ie. those which offer high security and high liquidity and satisfy the conditions set out below:

- investments denominated in pound sterling,
- investments due to be repaid within 12 months of arrangement,
- investments not defined as capital expenditure by legislation,
- invested with one of:
    - the UK Government,
    - a UK local Council, parish council or community council, or
    - a body or investment scheme of “high credit rating”, and
- investments where the principal sum to be repaid at maturity is the same as the initial sum invested, other than investments in the UK Government.

The Council, consistent with advice provided by Arlingclose, defines “high credit rating” organisations and securities 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. For money market funds and other pooled funds “high credit quality” is defined as those having a credit rating of A- or higher.

Non-specified Investments

Non-specified investments are those investments which do not, by definition, meet the requirements of a specified investment as set out above. They present a higher risk and therefore this Council does not intend to make any Non-Specified investments in 2019/20.

Investment Limits

The Council will invest surplus cash balances with each approved counterparty to a maximum of the greater of £3m or 30% of the overall investment, allocated in accordance with security, liquidity and yield. This includes cash sums placed in the investment account held with the Council’s corporate banking provider. However, the total balance held in the Council’s bank accounts may exceed these levels for a short period of time only (no longer than 4 working days) when:

- funding and income receipts are received into the bank account late in the day ie. after bank cut-off times have passed to enable funds to be placed with other approved counterparties; or
- investments are repaid into the bank account or availability of cleared funds is required to facilitate a large payment on a following day.

Treasury Management Indicators

Debt Related Treasury Activity Limits

The Council measures and manages its exposure to debt related treasury management risks using the following indicators and limits:

Interest rate exposure

This indicator is set to monitor the Council's exposure to the use of interest rate forecasts in its revenue budgets and shows the impact of a 1% rise or fall in interest rates.

Revenue budget impact of a 1%	2020/21	2021/22	2022/23
rise in interest rates – cost increases by	£62,499	£172,975	£308,377
fall in interest rates – cost reduces by	(£62,499)	(£172,975)	(£308,377)

Upper limits on variable and fixed interest rate exposure

These identify maximum limits for variable and fixed interest rates based upon the total debt position.

Interest rate exposures	2019/20	2020/21	2021/22	2022/23
Variable interest rate exposure - upper limit	30%	30%	30%	30%
Fixed interest rate exposure - upper limit	100%	100%	100%	100%

Maturity structure of borrowing.

These limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing within a short timeframe. Both upper and lower limits are set as follows:

Maturity structure of fixed interest rate borrowing	2019/20		2020/21	
	Lower Limit	Upper Limit	Lower Limit	Upper Limit
Under 12 months	0%	15%	0%	15%
12 months to 2 years	0%	15%	0%	15%
2 years to 5 years	0%	20%	0%	20%
5 years to 10 years	0%	30%	0%	30%
10 years and above	30%	90%	30%	90%

Investment Treasury Indicator

Principal sums invested for more than 364 days**.**

The purpose of this indicator is to control the Council's exposure to the risk of incurring losses by seeking early repayment of its investments. As it is not intended to enter into any non-specified investments, the Council is asked to approve the following limits:

	2019/20	2020/21	2021/22
Principal sums invested > 364 days	£nil	£nil	£nil

Other Items

There are a number of additional items that the Council is obliged by CIPFA or the DOE to include in its Treasury Management Strategy.

Policy on Use of Financial Derivatives

The Council will not use standalone financial derivatives (such as swaps, forwards, futures and options). Derivatives embedded into loans and investments, including pooled funds and forward starting transactions, may be used, and the risks that they present will be managed in line with the overall treasury risk management strategy.

Markets in Financial Instruments Directive (MiFID)

The Council has retained retail client status with its providers of financial services, including advisers, banks, brokers and fund managers, allowing it access to a smaller range of services but with the greater regulatory protections afforded to individuals and small companies. Given the size and range of the Council's treasury management activities, the Chief Financial Officer believes this to be the most appropriate status.

Investment Training

The Council recognises that investments, as well as wider treasury management issues require a high level of specialist knowledge. The Council will review staff training needs in respect of Treasury Management skills as part is its Pride in Performance Initiative and continuing professional development requirements. In addition, it is recommended that training should be provided for elected members to enable them to provide effective scrutiny of the strategy and to have the knowledge to make informed decisions.

Investment Advisers

Through a collaborative procurement process with the lead Council being Armagh City, Banbridge and Craigavon Borough Council, the Council has appointed Arlingclose Ltd as treasury mangement advisers. Whilst Arlingclose provides the Council with specific advice on investments, debt and capital finance issues, the Council recognises that responsibility for treasury management decisions remains with the organisation at all times and will ensure that undue reliance is not placed upon our external service providers.

ITEM 6

Ards and North Down Borough Council

Report Classification	Unclassified
Council/Committee	Special Council
Date of Meeting	11 February 2020
Responsible Director	Chief Executive
Responsible Head of Service	Head of Finance
Date of Report	07 February 2020
File Reference	FIN142
Legislation	Sections 4 and 6 Local Government Finance Act (NI) 2011
Section 75 Compliant	Yes ☒ No ☐ Not Applicable ☐
Subject	Robustness of Estimates and Adequacy of Reserves
Attachments	Appendix - forecast summary Balance Sheet

Background

Section 4 of the Local Government Finance Act 2011 requires the Chief Financial Officer of a council to submit a report on the robustness of the estimates and for the Council to have regard to this report when considering the estimates.

In addition, Section 6 requires the Chief Financial Officer of a council to submit a report on the adequacy of reserves and for the Council to have regard to this when considering the estimates.

Robustness of Estimates

The aim of the Medium-Term Financial Plan (MTFP) is to give the Council a realistic and sustainable plan that reflects the Council's priorities and the policy of reasonable Council Rate increases as reflected in the Corporate Plan.

The detailed estimates have been formulated in the context of newly agreed guiding principles and detailed work has been carried out with Directors, Heads of Service and Service Unit Managers for the various services. This work underpins the MTFP, taking into account forecast outturn, current spending plans and likely future demand level and pressures for both revenue and capital expenditure. A number of iterations have been reported to Corporate Services Committee during the estimates process, before being agreed at the special committee meeting on 6 February 2020.

The Chief Executive is satisfied that the Medium-Term Financial Plan and Budgets Report for 2020/21, encompassing the capital and revenue budget estimates for 2020/21, has been prepared in line with the CIPFA Treasury Management Code, Prudential Code and the Code of Practice on Local Authority Accounting and are robust.

Adequacy of Reserves

The Local Government Finance Act (NI) 2011 requires the Chief Financial Officer of a council to submit a report to council on the adequacy of any proposed level of financial reserves for a financial year.

The Medium-Term Financial Plan and Budget Report for 2020/21 (as presented at the Special Corporate Services Committee) considers the adequacy of the Council's financial reserves for the 2019/20 and 2020/21 financial years (as set out in the appendix). As set out in reports to the Corporate Services Committee, the Chief Executive notes the forecast General Fund balance and that the guiding principles agreed by Council in October 2019 set a clear path to increase the General Fund steadily over the coming four year period.

Cognisance has also been taken of the CIPFA Local Authority Accounting Panel Bulletin 99 (issued July 2014), which gives guidance on the level of reserves and the financing of Council expenditure.

The Chief Executive is content with the adequacy of the Council's forecast financial reserves for 2019/20 and 2020/21 as set out in the appendix.

RECOMMENDATION

It is recommended that Council note the report.

Appendix – Forecast Summary Balance Sheet

	Actual March 2019 £'000	Forecast March 2020 £'000	Budgeting March 2021 £'000
Long Term Assets	243,747	238,978	235,801
Cash	2,505	2,219	2,552
Other Current Assets	5,868	5,868	5,868
Short-Term Borrowing	(4,656)	(7,000)	-
Other Current Liabilities	(8,045)	(8,045)	(8,045)
Long Term Borrowing	(74,244)	(74,244)	(82,253)
Other Long-Term Liabilities	(32,733)	(32,733)	(32,733)
Net Assets	**132,442**	**125,043**	**121,190**
Capital Receipts Reserve	2,424	1,631	416
Capital Grants Unapplied Reserve	1,245	1,245	1,245
Revenue Grants Unapplied Reserve	713	713	713
Earmarked Fund	2,556	980	551
General Fund	3,422	2,625	3,140
Unusable Reserves	122,082	117,849	115,125
Net Worth	**132,442**	**125,043**	**121,190**