SOUTH YORKSHIRE PENSIONS AUTHORITY

16 MARCH 2017

Report of the Treasurer and the Interim Fund Director

TREASURY MANAGEMENT STRATEGY STATEMENT 2017/2018

1) Purpose of the report

To seek Members' approval of the treasury management procedures and strategy followed by the Authority.

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2) **Recommendation**

It is recommended that the Authority:-

a) **adopts the Annual Investment Strategy and recommendations set out in Appendix I; and**

b) **in accordance with Section 3(1) of the Local Government Act 2003 approves an Affordable Borrowing Limit, on a rolling basis for the forthcoming year and two successive years as outlined in Appendix II, of £250,000 being the maximum amount the Authority can afford to borrow; and**

c) **in accordance with the Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 approves the Minimum Revenue Provision Policy Statement (MRP) outlined in Appendix III; and**

d) **notes the list of counterparties used in Appendix IV; and**

e) **keeps the above under review.**

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3) Background information

3.1 Local authority treasury management activities are governed by Section 12 of Part I, Chapter I of the Local Government Act 2003 ("the Act") which provides that a local authority may invest "for any purposes relevant to its functions under any enactment, or for the purposes of the prudent management of its financial affairs". Pursuant to section 15 of the Act, in carrying out its functions, a local authority is required to have regard to relevant guidance and regulations issued by the Secretary of State and under the supporting Local Authorities (Capital Finance and Accounting) (England) Regulations 2003 to "have regard" to the Chartered Institute of Public Finance and Accounting (CIPFA) publication "Treasury Management in the Public

Services: Code of Practice and Cross-Sectoral Guidance Notes" ("the Code"). The Code was updated in November 2011 and covers the whole range of treasury management issues, including the fundamental principles for making and managing investments and requires local authorities to prepare an annual Treasury Management Strategy Statement ("TMSS"). Under the Code 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 the optimum performance consistent with those risks".

3.2 Amongst the primary requirements of the Code are the need to establish and maintain a Treasury Management Strategy Statement (TMSS) which sets out the policies and objectives of the Authority's treasury management activities and sets out how they will be achieved; approval of the Annual Investment Strategy (AIS); regular reporting on activities during the year and establishment of the delegation by the Authority of its responsibilities to other bodies and its officers. This report embodies the principles of the CIPFA Code and the Act and hence there is no separate TMSS published. For this Authority the delegated scrutinising body is the Corporate Planning and Governance Board and relevant monitoring reports are presented thereto.

3.3 The Authority manages its cash itself. The customised benchmark allocation for cash remains at 1.5% with a tactical range of 0%-10%. Some cash needs to be held in order to service creditors etc., pension payroll and potential currency hedging requirements. In absolute terms the amount of cash held at any one time might run to tens of millions of pounds but it is normally going to represent a relatively small percentage of total Fund assets. This is one reason why the CIPFA Code has not been universally adopted by Local Government Pension Scheme ("LGPS") administering authorities for the purposes of investing local authority pension funds. The specialised nature of pension fund monies does not lend itself easily to the Code: this is especially so since the funds themselves have no borrowing powers.

3.4 Apart from the occasional use of overdraft facilities the Authority has never utilised its borrowing powers granted under s1 of the Act. Nevertheless, the borrowing powers (i.e. in its own right and not on behalf of the Fund) are always reviewed annually and resolved upon separately by the Authority. The current governing legislation is the Act and the requirements are more fully referred to in section 4 below. Please note that the Act does not apply to pension funds, being controlled by a separate regulatory regime which is administered by the Department for Communities and Local Government (CLG).

3.5 Under the Local Government Pension Scheme (Management and Investment of Funds) Regulations 2016: SI 2016/946 ("the 2016 Regulations") an administering authority has a power to borrow on behalf of the LGPS fund it administers in certain circumstances (to pay benefits or meet investment commitments arising out of transition arrangements) subject to the sum borrowed and interest charged being repaid out of the fund within ninety days.

3.6 The management of the Fund itself is conducted in accordance with the Authority's Investment Strategy Statement which has been drawn up in accordance with extant Regulations.

3.7 Members were invited to attend a training session on treasury management matters, provided by Capita Asset Services, in January 2017.

3.8 As referred to in 3.2 above this report embodies the principles of the CIPFA Code and the Act and there is therefore no separate TMSS produced. Other relevant information referred to in this report is attached under the four following appendices: Appendix I, which is the Annual Investment Strategy (AIS); Appendix II is the Affordable Borrowing Limit (ABL); Appendix III is the Minimum Revenue Provision Policy Statement (MRP). The list of counterparties used is shown in Appendix IV.

4) <u>The Local Government Act 2003</u>

4.1 Section 1 of the Act grants the Authority its borrowing powers.

4.2 Although pension fund monies are specifically excluded from the investment regulations [The Local Authorities (Capital Finance and Accounting) (England) Regulations 2003] made under the Local Government Act 2003 Members should note that the Authority is subject to the capital expenditure requirements (Part 8, section 32). CLG will issue guidance under the Act from time to time and local authorities must have regard to the guidance.

4.3 Present guidance stresses the need for strategies to be prudent and defines a prudent investment policy as one having two objectives: achieving first of all security (protecting the capital sum from loss) and then liquidity (keeping the money readily available for expenditure when needed). The generation of investment income is distinct from these prudential objectives. In other words, the aim is to achieve an optimum return on investments commensurate with proper levels of security and liquidity. The Authority interprets this as meaning, firstly, security of capital; secondly, liquidity; thirdly, yield.

4.4 Section 3 (1) of the Act requires the Authority to set and keep under review an 'Affordable Borrowing Limit' (i.e. how much money it can afford to borrow) and to do so by reference to the CIPFA Prudential Code. The Limit is to be set, on a rolling basis, for the forthcoming year and two successive financial years. The Treasurer can confirm that the ABL has been kept under review.

4.5 Subsection (8) provides that a local authority's function under subsection (1) shall be discharged only by the authority; i.e. only Members can determine the affordable borrowing limit.

4.6 Because the Authority is a single purpose entity and not a local authority in the broader sense much of the Act does not apply directly to it. One of the grey areas appertains to the applicability of Part 1 of the Act, namely the prudential capital finance system called the prudential code for capital finance in local authorities. The key objectives of the "Prudential Code" are to ensure within a clear framework that:-

- capital investment plans of local authorities are affordable, prudent and sustainable

- treasury management decisions (notably borrowing for capital expenditure) are taken in a manner which supports affordability, prudence and sustainability

Affordability is implied in relation to the council tax. Prudence and sustainability is implied in relation to external borrowing.

4.7 Capital expenditure is generally interpreted as being expenditure incurred on assets which have a life expectancy of more than one year e.g. buildings, equipment, software. The Authority will, on occasion, purchase assets on behalf of the Fund to be used by the Fund e.g. software licences. Therefore, the Authority needs to demonstrate that it has fulfilled the objectives of the Prudential Code. The Code sets out the indicators that must be used and factors to be taken into account but does not include suggested limits or ratios as these are for the local authority to set. The prudential indicators for the forthcoming year and following years must be set before the beginning of the year. They may be revised at any time, following due process, and must be reviewed and revised, if appropriate, for the current year when the prudential indicators are set for the following year.

4.8 As already stated, in the case of this Authority it is almost certain that all capital expenditure will be incurred on behalf of the Fund, will be recharged to the Fund and, hence, financed by the Fund. The Authority has no power to borrow in order to finance this expenditure.

4.9 Under the Prudential Code Capital Prudential Indicators need to be set and local authorities need to monitor them. These are largely based upon the borrowing requirements and affordability. Because in this Authority’s instance the capital will be funded from revenue, most of the indicators are not relevant.

4.10 The Prudential Indicator for Capital Expenditure is a summary of the Authority’s capital expenditure plans. These are normally limited to the purchase of software licences or lease agreements.

4.11 The Minimum Revenue Provision (MRP) is a statutory charge relating to the repayment of debt arising from borrowing made to finance capital expenditure. The Local Authorities (Capital Finance and Accounting) (England) (Amendment) Regulations 2008 required that local authorities set MRP annually for approval before the start of the financial year to which the MRP relates and that it be “prudent”. There is no formal definition of “prudent”: therefore it’s up to the individual authority to determine this as part of their policy and to reflect it in the MRP charge that it sets. As in the case of the Authority, if there is no capital expenditure funded from borrowing, then there will not be an MRP charge. Nevertheless, a policy statement must be published in accordance with the statutory regulations. (Appendix III).

4.12 Section 5 of the LGA 2003 contains the power for an authority to borrow temporarily against future income yet to be received by it, provided the delayed receipt of such future income was not taken into account in the setting of the affordable borrowing limit. This power is thought to apply to the Authority by virtue of Regulation 32 of the Local Government (Capital Finance and Accounting) (England) Regulations 2003.

4.13 The Authority must have regard to both the guidance issued by CLG and the CIPFA Treasury Management Code when preparing its AIS. CLG recommends that the AIS be approved at the equivalent level of full council and should be approved before the start of the financial year. Under the current cycle of Authority meetings this meeting is the appropriate one. The AIS is included within the attached Statement.

4.14 The Authority's levy, issued in accordance with The Levying Bodies (General) Regulations 1992, finances the payment of statutory compensation and is not a function of capital financing decisions. The Authority does not enjoy a precept power.

4.15 Whilst the Authority has no need to undertake external borrowing the Act still appears to impose a duty to set an Affordable Borrowing Limit. Last year's ABL was set at £250,000 and there is not thought to be any need to amend that limit.

4.16 The Authority receives this report and approves policy and strategy but delegates management of the policy to the Corporate Planning and Governance Board which receives regular updates upon implementation and monitoring. Day to day management is entrusted to the Treasurer.

4.17 The Treasurer is the designated s73 Officer under the Local Government Act 1985 and has overall responsibility for the execution and administration of treasury management decisions and is responsible for, amongst other matters:

recommending clauses, treasury management policy/practices for approval, reviewing the same regularly, and monitoring compliance;

submitting regular treasury management policy reports;

receiving and reviewing management information reports;

reviewing the performance of the treasury management function;

ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function;

ensuring the adequacy of internal audit, and liaising with external audit;

the appointment of external service providers.

4.18 Under the Code the Treasurer is required to ensure that Members and officers with responsibility for treasury management receive adequate and appropriate training. Members were invited to a course in January 2017 provided by Capita Asset Services. The training requirements of officers are regularly reviewed.

4.19 The Authority utilises the services of external brokers and credit rating research published by Capita Asset Services. The Authority, however, recognises that responsibility for treasury management decisions remains with the organisation and sole reliance will not be placed on the use of external services. The Authority will also use market data and market information gleaned from other sources such as stockbrokers, the Bank of England, media and government.

4.20 In summary, therefore, the Authority employs a treasury management strategy in which investments are managed broadly in accordance with the Code of Practice for Treasury Management in Public Services published by CIPFA.

5) <u>Business banking services</u>

Lloyds Banking Group has been the Authority's "retail" bank since 1 April 2015.

6) <u>Implications</u>

6.1 Financial

There are no implications not otherwise mentioned within the report.

6.2 Legal

It is not thought that there are any legal implications.

6.3 Diversity

There are no diversity implications.

6.4 Risk

This Authority is the formal decision-making body for treasury management matters and has responsibility to ensure that adequate risk management processes are in place. This it discharges by agreeing a treasury management strategy and ensuring that compliance with it is regularly monitored by the Corporate Planning and Governance Board. There are potential reputational and financial risks that could arise from non-compliance with the Act and Regulations. It should also be noted that the ratings issued by credit rating agencies are only one means of assessing creditworthiness and are open to error and interpretation.

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Background papers used in the preparation of this report are available for inspection at the offices of the South Yorkshire Pensions Authority in Barnsley
Other sources and references: Bevan Brittan; CIPFA; CLG; LGA; Capita Asset Services, Bank of England