

# Special Governance Committee

Monday, 17th November,  
2014  
at 5.00 pm

## PLEASE NOTE TIME OF MEETING

Committee Room 1 - Civic Centre

This meeting is open to the public

### **Members of the Committee**

Councillor Burke (Chair)  
Councillor Chamberlain  
Councillor Daunt  
Councillor Inglis  
Councillor Keogh (Vice-Chair)  
Councillor Noon  
Councillor O'Neill

### **Independent Members**

Mr David Blake  
Mr Geoff Wilkinson

### **Contacts**

Head of Legal and Democratic Services  
Richard Ivory  
Tel. 023 8083 2394  
Email: [richard.ivory@southampton.gov.uk](mailto:richard.ivory@southampton.gov.uk)

Democratic Support Officer  
Pat Wood  
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## **PUBLIC INFORMATION**

### **Role of the Governance Committee**

Information regarding the role of the Committee's is contained in Part 2 (Articles) of the Council's Constitution.

#### [02 Part 2 - Articles](#)

It includes at least one Councillor from each of the political groups represented on the Council, and at least one independent person, without voting rights, who is not a Councillor or an Officer of the Council.

### **Public Representations**

At the discretion of the Chair, members of the public may address the meeting about any report on the agenda for the meeting in which they have a relevant interest.

### **Southampton City Council's Priorities:**

- .Jobs for local people
- Prevention and early intervention
- Protecting vulnerable people
- Affordable housing
- Services for all
- City pride
- A sustainable Council

**Smoking policy** – The Council operates a no-smoking policy in all civic buildings.

**Mobile Telephones:-** Please switch your mobile telephones to silent whilst in the meeting

**Use of Social Media:-** If, in the Chair's opinion, a person filming or recording a meeting or taking photographs is interrupting proceedings or causing a disturbance, under the Council's Standing Orders the person can be ordered to stop their activity, or to leave the meeting

**Access** – Access is available for disabled people. Please contact the Democratic Support Officer who will help to make any necessary arrangements.

**Fire Procedure** – in the event of a fire or other emergency a continuous alarm will sound and you will be advised by Council officers what action to take.

### **Dates of Meetings: Municipal Year 2014/15**

<b>2014</b>	<b>2015</b>
14 July	9 February
15 September	27 April
15 December	

## CONDUCT OF MEETING

### **Terms of Reference**

The terms of reference of the Governance Committee are contained in Part 3 of the Council's Constitution.

[03 - Part 3 - Responsibility for Functions](#)

### **Rules of Procedure**

The meeting is governed by the Council Procedure Rules as set out in Part 4 of the Constitution.

### **Business to be discussed**

Only those items listed on the attached agenda may be considered at this meeting.

### **Quorum**

The minimum number of appointed Members required to be in attendance to hold the meeting is 3.

## **DISCLOSURE OF INTERESTS**

Members are required to disclose, in accordance with the Members' Code of Conduct, **both** the existence **and** nature of any "Disclosable Pecuniary Interest" or "Other Interest" they may have in relation to matters for consideration on this Agenda.

### **DISCLOSABLE PECUNIARY INTERESTS**

A Member must regard himself or herself as having a Disclosable Pecuniary Interest in any matter that they or their spouse, partner, a person they are living with as husband or wife, or a person with whom they are living as if they were a civil partner in relation to:

- (i) Any employment, office, trade, profession or vocation carried on for profit or gain.
- (ii) Sponsorship:

Any payment or provision of any other financial benefit (other than from Southampton City Council) made or provided within the relevant period in respect of any expense incurred by you in carrying out duties as a member, or towards your election expenses. This includes any payment or financial benefit from a trade union within the meaning of the Trade Union and Labour Relations (Consolidation) Act 1992.

- (iii) Any contract which is made between you / your spouse etc (or a body in which the you / your spouse etc has a beneficial interest) and Southampton City Council under which goods or services are to be provided or works are to be executed, and which has not been fully discharged.

- (iv) Any beneficial interest in land which is within the area of Southampton.

- (v) Any license (held alone or jointly with others) to occupy land in the area of Southampton for a month or longer.

- (vi) Any tenancy where (to your knowledge) the landlord is Southampton City Council and the tenant is a body in which you / your spouse etc has a beneficial interests.

- (vii) Any beneficial interest in securities of a body where that body (to your knowledge) has a place of business or land in the area of Southampton, and either:

- a) the total nominal value for the securities exceeds £25,000 or one hundredth of the total issued share capital of that body, or
- b) if the share capital of that body is of more than one class, the total nominal value of the shares of any one class in which you / your spouse etc has a beneficial interest that exceeds one hundredth of the total issued share capital of that class.

## **Other Interests**

A Member must regard himself or herself as having an, 'Other Interest' in any membership of, or occupation of a position of general control or management in:

Any body to which they have been appointed or nominated by Southampton City Council

Any public authority or body exercising functions of a public nature

Any body directed to charitable purposes

Any body whose principal purpose includes the influence of public opinion or policy

## **Principles of Decision Making**

All decisions of the Council will be made in accordance with the following principles:-

- proportionality (i.e. the action must be proportionate to the desired outcome);
- due consultation and the taking of professional advice from officers;
- respect for human rights;
- a presumption in favour of openness, accountability and transparency;
- setting out what options have been considered;
- setting out reasons for the decision; and
- clarity of aims and desired outcomes.

In exercising discretion, the decision maker must:

- understand the law that regulates the decision making power and gives effect to it. The decision-maker must direct itself properly in law;
- take into account all relevant matters (those matters which the law requires the authority as a matter of legal obligation to take into account);
- leave out of account irrelevant considerations;
- act for a proper purpose, exercising its powers for the public good;
- not reach a decision which no authority acting reasonably could reach, (also known as the "rationality" or "taking leave of your senses" principle);
- comply with the rule that local government finance is to be conducted on an annual basis. Save to the extent authorised by Parliament, 'live now, pay later' and forward funding are unlawful; and
- act with procedural propriety in accordance with the rules of fairness.

## AGENDA

**Agendas and papers are now available via the Council's Website**

### **1 APOLOGIES**

To receive any apologies.

### **2 DISCLOSURE OF PERSONAL AND PECUNIARY INTERESTS**

In accordance with the Localism Act 2011, and the Council's Code of Conduct, Members to disclose any personal or pecuniary interests in any matter included on the agenda for this meeting.

NOTE: Members are reminded that, where applicable, they must complete the appropriate form recording details of any such interests and hand it to the Democratic Support Officer.

### **3 STATEMENT FROM THE CHAIR**

### **4 MINUTES OF PREVIOUS MEETING (INCLUDING MATTERS ARISING)**

(Pages 1 - 2)

To approve and sign as a correct record the Minutes of the meeting held on 15 September 2014 and to deal with any matters arising, attached.

### **5 MEMBERS' ALLOWANCE SCHEME (Pages 3 - 18)**

Report of the Head of Legal and Democratic Services seeking comments on the recommendations of the Independent Remuneration Panel on Members' allowances, attached.

### **6 TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMIT MID YEAR REVIEW 2014 (Pages 19 - 44)**

Report of the Chief Financial Officer regarding the Treasury Management Strategy and Prudential Limits Mid Year review, attached.

Friday, 7 November 2014

Head of Legal and Democratic Services

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## GOVERNANCE COMMITTEE

### MINUTES OF THE MEETING HELD ON MONDAY, 15 SEPTEMBER 2014

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#### Present:

Councillors Daunt (Except for Minutes 11-12), Inglis, Keogh (Vice-Chair), Noon and O'Neill

#### Independent Members

Mr David Blake and Mr Geoff Wilkinson

#### Apologies

Councillors Burke (Chair) and Chamberlain

### **COUNCILLOR KEOGH IN THE CHAIR**

#### 11. **DISCLOSURE OF PERSONAL AND PECUNIARY INTERESTS**

Mr Wilkinson declared a personal interest as a Southampton Member for Access in regard to Southampton City Council Complaints 2013/14.

#### 12. **MINUTES OF PREVIOUS MEETING (INCLUDING MATTERS ARISING)**

**RESOLVED:** that the minutes for the Committee meeting on 14 July 2014 be approved and signed as a correct record.

#### 13. **SOUTHAMPTON CITY COUNCIL COMPLAINTS 2013/14**

The Committee received and noted the report of the Head of Legal and Democratic Services regarding Complaints received and processed from July 2013 to March 2014.

The Committee expressed reluctance regarding the method of identifying complaints and collecting information and further expressed the desire to be confident of the process in future, although acknowledged that policy had been followed.

#### 14. **LOCALISM ACT 2011 - PROPOSAL FOR A PAN-HAMPSHIRE MEMBERS' CODE OF CONDUCT**

The Committee considered the report of the Head of Legal and Democratic Services seeking approval for a pan-Hampshire Members' Code of Conduct.

**RESOLVED** that a recommendation be made to Council that in the interests of achieving a consistent approach to Member Conduct across the HIOWLA authorities, the Members' Code of Conduct be amended to include provision regarding gifts and hospitality as set out in the report.

#### 15. **ANNUAL GOVERNANCE STATEMENT 2013-14**

The Committee considered the report of the Chief Financial Officer seeking to review the Annual Governance Statement 2013-14 and to note the status of the 2012-13 Action Plan.

**RESOLVED** that the Draft Annual Governance Statement 2013-14 be approved and that the status of the 2012-13 Action Plan be noted.

16. **FINANCIAL STATEMENTS FOR 2013/14**

The Committee considered the report of the Chief Financial Officer seeking approval for the financial statements for 2013/14.

**RESOLVED** that

- (i) the Statement of Accounts 2013-14 be signed subject to any changes required after the completion of the Audit; and
- (ii) any changes required to the draft accounts following completion of the annual audit be approved.

17. **INTERNAL AUDIT PROGRESS REPORT - AUGUST 2014**

The Committee received and noted the report of the Chief Internal Auditor regarding internal audit progress to the period August 2014.

It was noted that Members requested an email be sent listing “High” priority actions detailed within the report which were recorded as overdue.

18. **EXTERNAL AUDIT: ANNUAL RESULTS REPORT**

The Committee received and noted the report of the Chief Financial Officer regarding the external auditor’s ‘Audit Results Report’.



# Agenda Item 5

<b>DECISION-MAKER:</b>	GOVERNANCE COMMITTEE COUNCIL		
<b>SUBJECT:</b>	MEMBERS' ALLOWANCE SCHEME		
<b>DATE OF DECISION:</b>	17 NOVEMBER 2014 19 NOVEMBER 2014		
<b>REPORT OF:</b>	Head of Legal and Democratic Services		
<b><u>CONTACT DETAILS</u></b>			
<b>AUTHOR:</b>	<b>Name:</b>	<b>Richard Ivory, Head of Legal and Democratic Services</b>	<b>Tel:</b> 023 8083 2794
	<b>E-mail:</b>	<a href="mailto:richard.ivory@southampton.gov.uk">richard.ivory@southampton.gov.uk</a>	
<b>Director</b>	<b>Name:</b>	<b>Mark Heath, Director of Corporate Services</b>	<b>Tel:</b> 023 8083 2371
	<b>E-mail:</b>	<a href="mailto:mark.heath@southampton.gov.uk">mark.heath@southampton.gov.uk</a>	

## STATEMENT OF CONFIDENTIALITY

N/A

## BRIEF SUMMARY

Under the Local Government (Members Allowances) (England) Regulations 2003, local authorities are required to have Independent Remuneration Panels for the purpose of reviewing their schemes of Members' Allowances. Southampton City Council is required to review its scheme by September 2015 at the latest and have regard to the recommendations of the Independent Remuneration Panel.

## RECOMMENDATIONS:

### GOVERNANCE COMMITTEE

- |  |     |  |
|--|-----|--|
|  | (i) | To consider and comment on the recommendations of the Independent Remuneration Panel as set out on in the Panel's report (attached as appendix 1). |
|--|-----|--|

### COUNCIL

- |  |       |  |
|--|-------|--|
|  | (i)   | To consider the recommendations of the Independent Remuneration Panel as set out in the Panel's report (attached as Appendix 1); |
|  | (ii)  | To make any amendment to the Council's Constitution accordingly; and   |
|  | (iii) | To thank the members of the Independent Remuneration Panel for their work in reviewing the Members' Allowance Scheme.            |

## REASONS FOR REPORT RECOMMENDATIONS

- |    |   |
|----|---|
| 1. | Under the Local Authorities (Members Allowances) (England) Regulations 2003, Southampton City Council is required to have an Independent Remuneration Panel review the Members' Allowance Scheme within 4 years of the date that the scheme was approved. |
|----|---|

2.	Council last reviewed and approved the Members' Allowance Scheme on 14th September 2011. The Basic and Special Responsibility Allowances have not been revised since the scheme was approved in 2007.
3.	Council has a duty to have regard to the recommendations of the Independent Remuneration Panel when making or amending the scheme of allowances.
<b>ALTERNATIVE OPTIONS CONSIDERED AND REJECTED</b>	
4.	Council is required to approve a Members' Allowance Scheme by September 2015 in order to comply with The Local Authorities (Members' Allowances) (England) Regulations 2003. The options are:- (i) to approve the report of the Independent Remuneration Panel (ii) to amend the recommendations of the Independent Remuneration Panel (iii) to reject the recommendations of the Independent Remuneration Panel and consider alternative proposals.
<b>DETAIL (Including consultation carried out)</b>	
5.	The attached report (Appendix 1) of the Independent Remuneration Panel details the reasons and rationale for the recommendations made by the Panel.
6.	The Council is required by law to appoint an Independent Remuneration Panel, established for the purpose of considering the Members' Allowances, prior to making any decision to amend, revoke or replace the existing scheme of allowances. The recommendations of the Independent Remuneration Panel which met three times during October 2014 are set out in Appendix 1.
<b>RESOURCE IMPLICATIONS</b>	
<b><u>Capital/Revenue</u></b>	
7.	If all the recommendations set out in the report are implemented with a commencement date of 1 <sup>st</sup> April 2015, this will result in an ongoing annual saving of £15,000 from 2015/16. However this figure will need to be re-calculated if any variation or partial implementation is approved and the budget impact amended accordingly.
<b><u>Property/Other</u></b>	
8.	None
<b>LEGAL IMPLICATIONS</b>	
<b><u>Statutory power to undertake proposals in the report:</u></b>	
9.	Local Authorities (Members' Allowances) (England) 2003
<b><u>Other Legal Implications:</u></b>	
10.	None
<b>POLICY FRAMEWORK IMPLICATIONS</b>	
11.	None

**SUPPORTING DOCUMENTATION**

**Appendices**

1. Report of the Independent Remuneration Panel

**Documents In Members' Rooms**

1. None

**Equality Impact Assessment**

Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.

No

**Other Background Documents**

**Equality Impact Assessment and Other Background documents available for inspection at:**

Title of Background Paper(s)

Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)

1. None

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**A REVIEW OF  
MEMBERS' ALLOWANCES  
FOR  
SOUTHAMPTON CITY COUNCIL**

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**THE REPORT BY THE  
INDEPENDENT REMUNERATION PANEL**

**NOVEMBER 2014**

**South East Employers  
2 Crown Walk  
Jewry Street  
Winchester  
Hampshire  
S023- 8BB**

## **FOREWORD**

This report has been produced for Southampton City Council as part of the Council's requirement to receive independent advice from its statutory advisory panel on members' allowances. The membership of the Panel was David Gilani (Chair) Student Engagement Officer, University of Southampton, Mark Palmer, Development Director, South East Employers, Kevin Liles, Chair of Southampton Voluntary Services and Ellie Cawthera, Vice President Engagement, University of Southampton Students' Union.

The Panel would also like to record its gratitude to the Members and Officers of Southampton City Council who were interviewed or provided information for the Panel's consideration.

**Mark Palmer**  
**Member of the,**  
**Independent Remuneration Panel**

## **1. Introduction and Terms of Reference**

A review of the Southampton City Council Members' Allowances Scheme was conducted by the Independent Remuneration Panel at the request of the council in response to the requirement that all Councils are required to convene their Panel and seek its advice before they make any changes or amendments to their members' allowances scheme. The Panel was convened under The Local Authorities' (Members' Allowances) (England) Regulations (SI 1021) ("the 2003 Regulations')

The Panel met on the 23<sup>rd</sup> September, 2<sup>nd</sup> and 7<sup>th</sup> October 2014. The Panel interviewed the following Members and Officers as part of the review:

- Councillor Catherine McEwing – Chair of the Employment Panel
- Councillor Simon Letts- Leader of the Council
- Mark Heath – Director of Corporate Services
- Dawn Baxendale- Chief Executive
- Councillor Jeremy Moulton- Chair of the Overview and Scrutiny Management Committee
- Councillor Royston Smith- Opposition Group Leader and Leader of the Conservative Group
- Councillor Warwick Payne- Cabinet Member for Housing and Sustainability

Councillor Morrell (Group Leader- Councillors Against Cuts) was invited to interview but chose to decline the invitation.

## **2. Work of the Panel**

The remit of the Panel was to consider and review the Members' Allowance scheme. The Panel in particular reviewed the Allowance scheme in relation to the following:

- Basic Allowance
- Special Responsibility Allowances (SRA's)
- Allowances for Co-opted and Independent members of the Council committees and panels
- Criteria for travel and subsistence claims that needed to be reviewed.
- Communications allowance including telephone, broadband, mobile communications, IT hardware and software.
- Carers Allowance
- Matters related to the Member Allowance scheme that may be raised during the review process

The Panel requested information from officers to assist the review. Members were invited to give their views to the Panel on the allowance rates, ratios and differentials in the SRA's and other matters they wished to raise. Much of the consultation of the Members was undertaken by Group Leaders and shared with the Panel during the interview process.

The Panel met on three occasions and in coming to its recommendations, took into account the following:

- Current Members' Allowance Scheme
- The Local Authorities (Members' Allowances) (England) Regulations 2003
- Comparison data with similar unitary Councils regionally and nationally
- The role and responsibilities of the ward Member and those roles attracting a SRA
- Feedback from Members
- Councillor Census data produced by the Local Government Association (LGA). 2013 Census of Local Authority Councillors

- Comparison data in respect of the National Minimum Wage (NMW), The Living Wage (LW), Average Weekly Earnings and the National Joint Council (NJC) for Local Authorities pay rates/percentage increases.
- Other relevant information to support the Panels considerations and recommendations

### 3. Summary of recommendations

Following close consideration of the issues arising from their interviews with Members and Officers and other detailed information provided the Panel make the following recommendations:

- **Basic Allowance**

The Basic Allowance should be linked to the Living Wage (LW) as determined by the Living Wage Foundation. The current rate of the LW is £7.85 per hour (outside of London). The level of the LW is determined on an annual basis with the latest review having taken place on 3<sup>rd</sup> November 2014 as part of Living Wage Week. The Basic Allowance should be calculated on the basis of a non-Executive Member undertaking up to 27 hours on Council and group business.

The weekly hours are based using the Census of Local Authority Councillors 2013 (Local Government Association) which states that Councillors reported spending an average of 25.1 hours on council/group business and in metropolitan districts this increased to 30.9 hours. The recommendation of the Panel is based on a figure between 25.1 hours (that includes all councils including second tier districts and boroughs) and 30.9 hours for large urban metropolitan districts e.g. Leeds and Manchester MBC's.

The Basic Allowance based on the above criteria would be as follows £7.85 x 27 hours x 52 weeks = **£11,021.40**. This will be reviewed on an annual basis in line with the LW.

- **Special Responsibility Allowances (SRA's).**

The Special Responsibility Allowance (SRA'S) ratios should remain unchanged e.g. Leader of the Council 2 x Basic Allowance. The SRA's should be adjusted in line with changes to the Basic Allowance.

**The Chair of Governance Committee** should be added to the list of allowances for other committees. The Chair of Governance Committee should receive an SRA equal to the Chairs of other committees that is currently set at **0.5 x Basic Allowance**.

The criteria for determining the allowance for **Opposition Group Leaders** should be changed so that the level of allowance better reflects the size/number of Members in each group. The Panel recommends that a formula be introduced that is based on the number of Members within each Opposition Group.

Opposition Group Leaders should therefore receive an SRA equal to 1/24<sup>th</sup> of the Basic Allowance multiplied by the number of Members within the Group. The figure of 24 has been chosen as it is half (50%) of the current total of Council Members (48 Members). This approach ensures that the SRA for Opposition Group Leaders is never more than that of a Cabinet Member (i.e. an amount equal to the Basic Allowance). The approach is both equitable and will lead to financial savings from what is currently spent on SRA's for Opposition Group Leaders.



The figures will be as follows £11,021.40 divided by 24 = **£459.23 per Group Member**. Based on the current Council political composition this will be equate to the following level of allowance:

- Conservative Group Leader - £459.23 x 18 Members = **£8266.14**
- Councillor's Against Cuts Group Leader- £459.23 x 2 Members = **£918.46**

- **Co-opted Member/Independent Persons Allowance**

The Co-opted Member/Independent Persons Allowance to be de- linked from the National Minimum Wage and to be increased in line with National Joint Council (NJC) pay awards.

The allowance is **£643.80** and is calculated on the basis of members working for up to 3 weeks at 37 hours per week on an hourly rate based on the 2007 National Minimum Wage. The Panel were of the view that the figure of £643.80 should remain but it be separated from the National Minimum Wage and any future increases be linked to the NJC pay awards for Local Government Employees (A pay award is currently pending and is likely to be 2.2% from 1<sup>st</sup> January 2015 to 31<sup>st</sup> March 2016) .

- **Carers' Allowance**

The Panel are of the view that the current allowance for Carers' of a maximum of £15.00 per day is no longer fit for purpose and should be replaced by a more realistic allowance. The Panel recommend that the Carers' Allowance be increased so that claims can be made up to that of the **Living Wage £7.85 per hour** on provision of receipts. Payment will be made for actual approved Councillor Duties only and will also include reimbursement of payment for travel time.

- **Communications Allowance**

The current allowance for telephone line rental and broadband (£10.20 per month line rental/ £15.00 per month line rental and broadband) should continue until the Councils Transformation Review of Communications is completed. Once a new framework for Council Communications is in place then the Council should request that the Panel consider an appropriate set of allowances to cover all aspects of communication e.g. telephone line rental, broadband, IT hard ware/software and mobile communications.

**All other elements of the Members' Allowances scheme to remain unchanged**

#### **4. Implementation of Recommendations**

**As permitted by the 2003 Members' Allowances Regulations (paragraph 10.6) it is recommended that the new Members' Allowances scheme as recommended in this report be implemented by the 1<sup>st</sup> April 2015.**

#### **5. Considerations and Recommendations of the Panel**

##### **A. Basic Allowance**

The Members' Allowance scheme was last reviewed in August 2011 with the report been considered by Council in September 2011. Many of the Panels recommendations were either not accepted or amended by Members.

The Council had decided to use the National Minimum Wage (NMW) as the basis of the Basic Allowance, based on a 37 hour week, with the SRA's being proportional to the Basic Allowance. Although the use of the NMW as the basis for calculating the Basic Allowance had been sustainable concern was expressed by the Panel that the current

allowance was still based on the NMW rate of 2009 and the Basic and SRA's had not increased in line with the increase in the NMW.

The Panel are of the view that the NMW is no longer the best criteria for determining the Basic Allowance and that a more appropriate criteria for determining the Basic Allowance is the Living Wage (LW). The Council is currently in the process of negotiating the use of the LW for Council employees and is also committed to encouraging employers across the city to commit to the LW as a basis for 'fair' pay. The use of the LW as the basis for determining the level of Basic Allowance will provide a medium term and sustainable approach for the Members' Allowance scheme.

Whilst the Panel appreciated that the current link to the NMW was based on a 37 hour week the Panel did not feel that this reflected the actual number of hours that a non-Executive Member should be undertaking to effectively carry out the role. Although it was acknowledged that the actual number of hours undertaken would be different for each Member and would be determined by the ward represented and other responsibilities e.g. other employment or caring responsibilities; it was felt that 37 hours was excessive.

The view of the Panel in relation to the weekly hours was supported by both feedback from the interviews and also the findings of the Census for Local Authority Councillors 2013 (LGA). The Census reported that the average number of hours per week on council, group and party business was 25.1 hours. This figure increased to 30.9 hours for Members in large metropolitan councils e.g. Sheffield, Manchester and Leeds and fell to 20.6 hours in shire district councils. As a mid size unitary 'all purpose' council the Panel are of the view that 27 hours per week is a good basis for determining the Basic Allowance.

The recommended Basic Allowance for the Council also compares favourably with other mid size unitary councils. (The figures are based on 2013/14 Basic Allowances).

<b>Council</b>	<b>Basic Allowance (£'s)</b>
Brighton & Hove	11,463
Bristol City	11,530
Coventry City	13,001
Derby	9,976
Doncaster	12,120
Hull City	12,337
Milton Keynes	9,962
Plymouth City	10,044
Portsmouth City	10,302
<b>Southampton City</b>	<b>11,021 (Recommended Basic Allowance)</b>
Stoke- on –Trent	11,876
Sunderland City	8,369
Wakefield MBC	11,095

**Recommendation:** That the Basic Allowance be calculated based on the use of the LW currently **£7.85 per hour** (2014-15). The LW is currently reviewed on an annual basis during Living Wage Week (first week in November each year). The Basic Allowance to be calculated on the basis of Members' undertaking an average of **27** hours per week on

council, group and party business. The recommended Basic Allowance is £7.85 x 27 hours x 52 weeks = **£11,021.40**.

## **B. Special Responsibility Allowances**

The Panel noted that the Council had determined to base the SRA's using a multiplier of the Basic Allowance. The Panel continues to support this approach as the basis for calculating the level of SRA's to be paid.

The Panel also continues to support the current multipliers for the following roles:

Leader of the Council	-	2 x Basic Allowance
Cabinet Member	-	1x Basic Allowance
Chair of Employment	-	0.5 x Basic Allowance
Chair of OSMC	-	0.5 x Basic Allowance
Chair of Planning	-	0.5 x Basic Allowance
Chair of Licensing	-	0.5 x Basic Allowance
Chair of Health Panel	-	0.25 x Basic Allowance

### **Chair of Governance Committee**

The Panel considered the allowance for the Chair of Governance Committee that since been set up has had no allowance and is currently not included in the scheme of allowances. When the Committee was first developed the Chair was the Mayor and therefore there was no SRA entitlement. However, in the last few years following statutory changes the Chair has become a Member and the Panel are therefore of the view that the role of Chair of Governance Committee should receive a SRA at a rate similar to the other main committees.

**Recommendation:** That the Chair of Governance Committee receive a SRA equal to the other main committees, **0.5 of the Basic Allowance, £5,510.70**.

### **Chair of Children and Families Scrutiny Panel**

The Panel are aware that the Overview and Scrutiny Management Committee had in October 2014 approved the setting up of a Children and Families Scrutiny Panel for 2 years to provide robust scrutiny of Children and Family services. The Panel should lead to a strengthening of the political scrutiny of these sensitive and complex areas; and ensure that the necessary rigour to the scrutiny of Children and Families is undertaken.

The Panel recommends that the Chair of Children and Families Scrutiny Panel receive a SRA comparable to the Health Scrutiny Panel, 0.25 x Basic Allowance.

**Recommendation:** The Panel recommends that the Chair of Children and Families Scrutiny Panel receive a SRA 0.25 X Basic Allowance **£2,755.36**.

### **Opposition Group Leaders**

The current allowance for Opposition Group Leaders is currently 0.75 x Basic Allowance £8,369.40 and the Panel are of the view that the allowance for Opposition Group Leader needs to better reflect the size of the political group. The Panel recognise that it is a critically important role to organise, manage and develop a political group and the role also supports local democracy and local accountability.

However, the complexity of the role of Opposition Group Leader is impacted by the size of political group that the Leader has to oversee. In the recent past the size of the political group

was less of an issue since the main opposition groups were of roughly similar size, however this is no longer the case and the current two opposition groups are of a comparably different size.

The Panel are of the view that the Opposition Group Leader should receive a SRA based on the number of Members within the group and this should be based on a per Member payment. The Panel are also of the view that the Leader of the Opposition Group should not receive a SRA greater than that of a Cabinet Member (1x Basic Allowance) since the Cabinet Members are the key decision makers.

The Panel recommends that the Opposition Group Leaders should receive a SRA equal; to 1/24<sup>th</sup> the Basic Allowance multiplied by the number of Members within their group. The figure 24 is chosen as it is half (50%) the number of all Members (48 Members). This ensures that the SRA for Opposition Group Leader is never more than that of a Cabinet Member (i.e. an amount equal to 1 x Basic Allowance)

**Recommendation:** The Panel recommends that the SRA for the Opposition Group Leaders be based on the size of the opposition group. Each Opposition Group Leader should receive an allowance equal to 1/24<sup>th</sup> the Basic Allowance multiplied by the number of Members within the Group. This will need to be reviewed after each election, by-election or should there be a vacancy in a ward or a defection to another party.

The current recommended Opposition Group Leader allowances are as follows:

**Conservative Group Leader** – 18 Members x £459.23 per Group Member = **£8,266.14**  
**Councillors Against Cuts Group Leader** – 2 Members x £459.23 per Group Member = **£918.46.**

### **Deputy Leader**

In accordance with the Local Government and Public Involvement in Health Act 2007, the Council Leader is required to appoint a Deputy. The Panel considered whether a SRA should be paid to the Deputy Leader.

**Recommendation:** The Panel recommend that as the role of the Deputy Leader has always been a Cabinet Member and has received a SRA for the Cabinet Member role then their should be no separate allowance for the role of Deputy Leader.

### **C. Co-optees' and Independent Persons Allowance**

There are currently co-optees on two committees who are entitled to the allowance of **£643.80** per annum. The two committees are:

- Governance Committee- There are two co-opted independent members of the Committee who are members of the public , openly recruited to serve a three year term
- Overview and Scrutiny Management Committee (OSMC) – There are four co-optees, two church representatives and two governor representatives who are only entitled to vote on educational matters. The appointments are statutory but changes to the committee structure have impacted on the nature and level of their participation.

The Panel are of the view that the current allowance of £643.80 for the co-optees should be left unchanged but the basis by which the allowance is calculated should be changed. The current Co-optee allowance is calculated based on the equivalent of three weeks of the NMW, with a week based on 37 hours. The level of allowance is based on the NMW rate at 2007 and has not been increased in line with the increase in the NMW. The Panel are of the view that the link between the Co-optee allowance and the NMW should be broken as it has failed to be up rated in line with the NMW. The Co-optee allowance should no longer be

linked to the NMW but should be increased in line with the NJC pay award for Local Government Employees.

**Recommendation:** The current rate of the Co-optee allowance should continue at **£643.80** per annum but the link to the NMW should be broken. Future increases in the Co-optee allowance should be linked to the NJC pay award for Local Government Employees. It is anticipated that this will lead to an increase in the Co-optees allowance of 2.2% for the period 1<sup>st</sup> January 2015 to 31<sup>st</sup> March 2016

The Localism Act 2011 specifies that “Arrangements” should be adopted by the Council for dealing with allegations that a Member may have breached the Code of Conduct. Provision should be made for the appointment of a **Designated Independent Person**. The Council currently has two Independent Persons that receive an allowance of **£643.80 per annum**. The allowance is the same as that of the Co-optees and is currently calculated on the same basis e.g. Three weeks of the NMW at 37 hours per week.

**Recommendation:** The current rate of the Designated Independent Persons Allowance should continue at **£643.80** per annum but the link to the NMW should be broken. Future increases in the Designated Independent Persons Allowance should be linked to the NJC pay award for Local Government Employees.

#### **D. Carers Allowance**

The Council currently has a structure of allowances for carers that is both insufficient, out of date and as a result is not widely used by Members. The Panel are aware that there was a significant difference in how the Council support staff with childcare responsibilities (e.g. childcare vouchers funded from employees’ gross salary) and that there was no staff scheme for a carers’ allowance. Therefore based on the existing and out of date rates, the maximum amount that could be paid for childcare currently does not exceed £15 per day and this is the provision in the current Members’ Allowances scheme.

The Panel are of the view that this is an insufficient amount for a Member with caring responsibilities to undertake the ‘approved duties’ of an Elected Member. The current Carers’ allowance could also act as a barrier to members of the public considering standing for Council if the cost of care is not wholly or mostly met by the Council.

With regard to the Carers’ allowance the Panel are of the view that the allowance should meet a significant amount of the cost for care that is charged by the commercial organisations, based on an hourly rate.

**Recommendation:** The current allowance of £15 per day to be replaced with an allowance based on an hourly rate. The hourly rate for supporting care responsibilities should be linked to the **Living Wage, currently £7.85 per hour**. Payment for caring responsibilities will support all current ‘Approved Duties’ for claiming expenses and will be reimbursed on production of receipts to a maximum of the rate of the LW £7.85 per hour. The allowance payment will also cover the travel time incurred by the Member in carrying out approved duties.

#### **E. Communications**

The Council’s current policy and approach to communications that includes telephone, mobile communication, broadband and IT software and hardware is currently been reviewed as part of the Council’s Transformation Programme. The recommendations of the review of communications will apply to both Council employees and Elected Members.

The current Members' Allowances scheme in respect of communications is the same as that provided for employees; telephone line rental is reimbursed at a rate of £10.20 per month and for Members that have both a telephone line rental and internet broadband access the maximum payment is £15.00 per month.

The Panel are of the view that the current allowance in terms of its scope e.g. the current lack of an allowance for and the provision of a mobile/ smartphone and/or a lap top or tablet computer was unacceptable and could be a barrier to a Member carrying out the role effectively.

However, the Panel are aware of the current review of communications as part of the Transformation Programme and recognise that at the moment it would not be right to make any changes to the current scheme of allowances until the review recommendations have been agreed and implemented. Once the review recommendations have been agreed and implemented the Panel would like to meet to determine a more appropriate set of allowances to cover all aspects of communication.

**Recommendation:** The current allowance of **£10.20 per month** for telephone line rental and **£15.00 per month** for telephone line rental and broadband to remain unchanged until the approved recommendations of the Transformation Programme in respect of communications are implemented. Once the recommendations of the Transformation Programme review are implemented then the Panel will reconvene to recommend a more relevant and up to date approach to allowances to support all aspects of modern communication.

#### **F. Travel and Subsistence.**

The Members' Allowances scheme reimburses travel by car at the HMRC Approved Mileage Allowance Payment. Subsistence rates for undertaking 'Approved Duties' are adjusted in line with the rate for City Council employees. The Panel **recommends** that the current approach to travel and subsistence rates continues and is adjusted in line with the rate for Council employees.

#### **6. Implementation of the Recommendations**

**As permitted by the 2003 Members' Allowances Regulations (paragraph 10.6) it is recommended that the new Members' Allowances scheme as recommended in this report is implemented from 1<sup>st</sup> April 2015.**

**Appendix 1**

**Recommendations of the Panel – Members’ Allowance Scheme**

<b>Allowance Scheme</b>	<b>Current Allowance (£) 2009 rate payable</b>	<b>Recommended Allowance (£)</b>	<b>Recommended Allowance Calculation</b>
Basic Allowance	11,159.20	11,021.40	Living Wage x 27hours x 52 weeks
Leader of the Council	22,318.40	22,042.80	2 x Basic Allowance
Cabinet Member	11,159.20	11,021.40	1 x Basic Allowance
Chair of Employment	5,579.60	5,510.70	0.5 x Basic Allowance
Chair of Planning	5,579.60	5,510.70	0.5 x Basic Allowance
Chair of Licensing	5,579.60	5,510.70	0.5 x Basic Allowance
Chair of OSMC	5,579.60	5,510.70	0.5 x Basic Allowance
Chair of Health Scrutiny Panel	2,789.80	2,755.36	0.25 x Basic Allowance
Chair of Children and Families Scrutiny Panel		2,755.36	0.25 x Basic Allowance
Opposition Group Leaders	8,369.40	459.23 per Group Member	Based on a per Group Member figure (1/24 <sup>th</sup> of the Basic Allowance)
Co-opted Member	643.80	643.80	To increase in line with NJC pay awards
Chair of Governance Committee (replaces Audit Committee Chair)		5,510.70	0.5 x Basic Allowance
Independent Persons (Two)	643.80	643.80	To increase in line with NJC pay awards
Carers Allowance	15. 00 per day	7.85 per hour	To be linked to Living Wage. Per hour of approved duties plus travel time
Communications	15.00	15.00	Per month
Travel	45p	45p	HM Revenue and Customs Rate. Per mile for the first 10,000 miles

**Note:**

Basic Allowance = Living Wage x 27 hours per week x 52 weeks a year

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# Agenda Item 6

<b>DECISION-MAKER:</b>	GOVERNANCE COMMITTEE COUNCIL		
<b>SUBJECT:</b>	TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS MID YEAR REVIEW 2014		
<b>DATE OF DECISION:</b>	17 NOVEMBER 2014 19 NOVEMBER 2014		
<b>REPORT OF:</b>	CHIEF FINANCIAL OFFICER		
<b><u>CONTACT DETAILS</u></b>			
<b>AUTHOR:</b>	<b>Name:</b>	Andrew Lowe	<b>Tel:</b> 023 8083 2049
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## STATEMENT OF CONFIDENTIALITY

N/A

## BRIEF SUMMARY

The Council approved a number of indicators at its meeting of the 12 February 2014. Following the September update of the Capital Programme and an analysis of Treasury Management activity in 2013/14 and between April and September 2014, these indicators have been reviewed for 2014/15 and are reported in accordance with CIPFA's code of practice on Treasury Management, (the "CIPFA TM Code"), and in line with the approved Treasury Management Strategy (TMS).

The core elements of the 2014/15 strategy are :

- To continue to make use of short term variable rate debt to take advantage of the current market conditions of low interest rates.
- To constantly review longer term forecasts and to lock into longer term rates through a variety of instruments as appropriate during the year, in order to provide a balanced portfolio against interest rate risk.
- To secure the best short term rates for borrowing and investments consistent with maintaining flexibility and liquidity within the portfolio.
- To invest surplus funds prudently, the Council's priorities being:
  - Security of invested capital
  - Liquidity of invested capital
  - An optimum yield which is commensurate with security and liquidity.
- To approve borrowing limits that provide for debt restructuring opportunities and to pursue debt restructuring where appropriate and within the Council's risk boundaries.

With overall annual expenditure in excess of £600M and an extensive capital programme, the Council is required to actively manage its cash-flows on a daily basis. The requirement to invest or to borrow monies to finance capital programmes, and to cover daily operational needs is an integral part of daily cash and investment portfolio management.

## **RECOMMENDATIONS:**

### **GOVERNANCE COMMITTEE**

- i) To note the current and forecast position with regards to these indicators and endorse any changes;
- ii) To note that the continued proactive approach to Treasury Management (TM) has led to reductions in borrowing costs and safeguarded investment income during the year whilst increasing the yield; and
- iii) To endorse the increase in the non-specified investment limit for institutions falling below our minimum limit investment limit A- be increased to £5M, as detailed in paragraph 29.

### **COUNCIL**

- i) To approve any changes to the Council's Prudential Indicators as detailed within the report;
- ii) Continue to delegate authority to the Chief Financial Officer, following consultation with the Cabinet Member for Resources to approve any changes to the Prudential Indicators or borrowing limits that will aid good treasury management. For example increase the percentage for variable rate borrowing to take advantage of the depressed market for short term rates. Any amendments will be reported as part of quarterly financial and performance monitoring and in revisions to this strategy;
- iii) To note that the continued proactive approach to Treasury Management (TM) has led to reductions in borrowing costs and safeguarded investment income whilst increasing the yield; and
- iv) To approve the increase in the non-specified investment limit for institutions falling below our minimum investment limit of A- be increased to £5M, as detailed in paragraph 29.

### **REASONS FOR REPORT RECOMMENDATIONS**

1. The TM Code requires public sector authorities to determine an annual TM Strategy and now, as a minimum, formally report on their treasury activities and arrangements to full Council mid-year and after the year-end. These reports enable those tasked with implementing policies and undertaking transactions to demonstrate they have properly fulfilled their responsibilities, and enable those with ultimate responsibility/governance of the TM function to scrutinise and assess its effectiveness and compliance with policies and objectives.

### **ALTERNATIVE OPTIONS CONSIDERED AND REJECTED**

2. No alternative options are relevant to this report.

## DETAIL (Including consultation carried out)

### CONSULTATION

3. The capital programme update on which this report is based has been subject to its own consultation processes.

### BACKGROUND

4. The Chartered Institute of Public Finance and Accountancy's Treasury Management Code (CIPFA's TM Code) requires that authorities report on the performance of the treasury management function at least twice yearly (mid-year and at year end). The Authority's Treasury Management Strategy for 2014/15 was approved by full Council on 12 February 2014, item 87, which can be accessed on <http://www.southampton.gov.uk/modernGov/ieListDocuments.aspx?CId=122&MId=2469&Ver=4>

The Authority has borrowed and invested substantial sums of money and is therefore exposed to financial risks including the loss of invested funds and the revenue effect of changing interest rates. This report covers treasury activity and the associated monitoring and control of risk.

5. In essence TM can always be seen in the context of the classic 'risk and reward' scenario and following this strategy will contribute to the Council's wider TM objective which is to minimise net borrowing cost short term without exposing the Council to undue risk either now or in the longer in the term.
6. Treasury management 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."*
7. Overall responsibility for treasury management remains with the Council. No TM activity is without risk; the effective identification and management of risk are integral to the Council's treasury management objectives. The main risks to the Council's treasury activities are:
  - Liquidity Risk (Inadequate cash resources)
  - Market or Interest Rate Risk (Fluctuations in interest rate levels and thereby in the value of investments).
  - Inflation Risks (Exposure to inflation)
  - Credit and Counterparty Risk (Security of Investments)
  - Refinancing Risks (Impact of debt maturing in future years).
  - Legal & Regulatory Risk (i.e. non-compliance with statutory and regulatory requirements, risk of fraud).
8. This report:
  - a) is prepared in accordance with the revised CIPFA Treasury Management Code and the revised Prudential Code,
  - b) presents details of capital financing, borrowing, debt rescheduling and investment transactions,
  - c) reports on the risk implications of treasury decisions and transactions,
  - d) gives details of treasury management transactions during 2014/15 to date, and

e) confirms compliance with treasury limits and Prudential Indicators.

## BORROWING REQUIREMENT AND DEBT MANAGEMENT

9. The underlying need to borrow for capital purposes is measured by the Capital Financing Requirement (CFR). The CFR, together with balances and useable reserves, are the core drivers of TM Activity. This was estimated at £446M as at the 31/03/2015 when the TM strategy was approved and has been revised down to £431M following a revision of the capital programme and adjusting for 2013/14 actual position.
10. The Authority is able to borrow funds in excess of the current level of its CFR up to the projected level in 2016/17 (£439M). The Authority is likely to only borrow in advance of need if it felt the benefits of borrowing at interest rates now compared to where they are expected to be in the future, outweighs the current cost and risks associated with investing the proceeds until the borrowing is actually required.
11. The forecast movement in coming years is one of the Prudential Indicators (PIs). The movement in actual external debt and usable reserves combine to identify the Authority's borrowing requirement and potential investment strategy in the current and future years and is shown in the tables below together with activity in the year.

	Balance on 01/04/2014	Debt Maturing or Repaid	New Borrowing	Balance as at 30/9/2014	Increase/ (Decrease) in Borrowing for Year	Average Life / Average Rate %	
	£M	£M	£M	£M	£M	Life	%
Short Term Borrowing	10	(10)	0	0	(10)	23 Years	3.20
Long Term Borrowing	264	(6)	0	258	(6)		
<b>Total Borrowing</b>	<b>274</b>	<b>(16)</b>	<b>0</b>	<b>258</b>	<b>(16)</b>		

\*Please note that these figures do not reflect the accounting convention of moving loans maturing in the year from long term to short term

	31-Mar-14 Actual	31-Mar-15 Approved	Current Portfolio	31-Mar-15 Current Estimate	31-Mar-16 Current Estimate	31-Mar-17 Current Estimate
	£M	£M	£M	£M	£M	£M
<b>External Borrowing:</b>						
Fixed Rate – PWLB Maturity	139	148	139	139	167	204
Fixed Rate – PWLB EIP	81	81	75	69	58	46
Variable Rate – PWLB	35	35	35	35	35	35
Variable Rate – Market	9	9	9	9	9	9
<b>Long Term Borrowing</b>	<b>264</b>	<b>273</b>	<b>258</b>	<b>252</b>	<b>269</b>	<b>294</b>
<b>Short Term Borrowing</b>						
Fixed Rate – Market	10	10	0	20	30	40
<b>Other Long Term Liabilities</b>						
PFI / Finance leases	62	61	62	67	65	62
Deferred Debt Charges	16	17	16	16	15	14
<b>Total Gross External Debt</b>	<b>352</b>	<b>361</b>	<b>336</b>	<b>355</b>	<b>379</b>	<b>410</b>
<b>Investments:</b>						
Deposits and monies on call and Money Market Funds	(66)	(40)	(73)	(40)	(40)	(40)
Financial Instruments	(3)	(3)	(6)	(13)	(13)	(13)
<b>Total Investments</b>	<b>(69)</b>	<b>(43)</b>	<b>(79)</b>	<b>(53)</b>	<b>(53)</b>	<b>(53)</b>
<b>Net Borrowing Position</b>	<b>283</b>	<b>318</b>	<b>258</b>	<b>302</b>	<b>326</b>	<b>357</b>

### **Public Works Loan Board (PWLB) Borrowing**

12. The PWLB remains the Council's preferred source of long term borrowing given the transparency, flexibility and control it offers.

### **PWLB Certainty Rate**

13. The Council successfully qualified for borrowing at the 'Certainty Rate', (0.20% below the PWLB standard rate) following the submission of the Certainty Rate form to the Department of the Environment, which included details of the capital expenditure and borrowing plans for the Council over the next three years. In April the Council submitted a further application along with the 2014/15 Capital Estimates Return to access this reduced rate for a further 12 month period from 1 November 2014.

### **Loans at Variable Rates**

14. Included within the PWLB portfolio is £35M of variable rate loans, which are currently averaging 0.58% and are helping to keep overall borrowing costs down. Whilst in the current climate of low interest rates this remains a sound strategy, the Council need to review these regularly and if appropriate switching into fixed rate loans.
15. In order to mitigate these risks further, the Council approved the creation of an Interest Equalisation Reserve in 2009 to help manage volatility in the future and ensure that there was minimal impact on annual budget decisions or council tax in any single year. At that point a major debt restructuring exercise had taken place in order to take advantage of market conditions and produce net revenue savings. As reported in the outturn report in preparation of the banking regulation reform, this reserve was renamed 'Treasury Risk Reserve' to recognise the wider risk. The level of this reserve is reviewed on a regular basis.

### **Internal Borrowing**

16. Given the significant reductions to local government funding putting pressure on Council finances, the strategy followed was to minimise debt interest payments without compromising the longer-term stability of the portfolio. The differential during 2013/14 between the cost of new longer-term debt (3.18% average rate for a 20 year PWLB fixed rate maturity) and the return generated on the Council's temporary investment returns was significant (2.4%).
17. As at the 31 March 2014 the Council used £73M of internal resources in lieu of borrowing which has been the most cost effective means of funding past capital expenditure to date. This has lowered overall treasury risk by reducing both external debt and temporary investments. However, this position will not be sustainable over the medium to long term and the Council will need to borrow to cover this amount as balances fall. Following the latest update of the Capital Programme, approved by Council in September 2014, the Council is expected to borrow up to £74M between 2014/15 and 2016/17. Of this £40M relates to new HRA capital spend (GF has no new requirement at this stage) and the remainder to the refinancing of existing debt and externalising internal debt to cover the expected fall in balances.
18. However due to the continued and increased uncertainty in the markets and the expectations of interest rates staying lower for longer it may be appropriate to

maintain the council use of internal resources for part or all of this amount; providing that balances can support it. No long term borrowing has been taken to date and is none is expected to be taken until the third quarter of the year and will be assessed in conjunction with the development of the capital programme, cash balances and advice from the Council's treasury advisor.

### **INVESTMENT ACTIVITY**

19. The Authority holds significant invested funds, representing income received in advance of expenditure plus balances and reserves held. There has been an increase in balances since the beginning of the year (£66M), peaking at £125M in mid- May. Based on previous years balances this is expected to fall around December when we have traditionally needed to borrow short term from the money markets due to uncertainty on the capital programme and the need to borrow long term. Projected balances to the end December indicate that on present levels of spend we should have about £20m more than this time last year, around £60M, so unless there is significant capital spend between now and then, there should be no need to borrow short term unless we feel this is prudent to protect our investments in the higher returning call accounts.
20. The Guidance on Local Government Investments in England gives priority to security and liquidity and the Council's aim is to achieve a yield commensurate with these principles. Security of capital has remained the Council's main investment objective. This has been maintained by following the Council's counterparty policy as set out in its TM Strategy Statement for 2014/15.
21. Counterparty credit quality is assessed and monitored with reference to: Credit Ratings. The Council's minimum long-term counterparty rating is A- (or equivalent across rating agencies Fitch, S&P and Moody's); credit default swaps; financial statements, information on potential government support and reports in the quality financial press.

### **Externally Managed Investments**

22. On the 1 April the Council invested £5M in property funds which offer the potential for enhanced returns over the longer term, but may be more volatile in the shorter term. These funds are managed by professional fund managers which allows the Authority to diversify into asset classes other than cash without the need to own and manage the underlying investments. This investment has returned an average of £20k per month, which will generate an additional £200k for the year. Consideration is also being given on whether to invest an additional £1M in the fund as the yield is attractive but this will increase our risk. The value of the fund at 30th September was £4,947,879, a "loss" of £52k against initial investment. Even allowing for this the fund still returned a yield of 3.67%.

### **Internally Managed Investments**

23. The rolling programme of yearly investments has been stopped due to lower balances last year and the difficulty in placing at attractive rates, plus we are preparing for lower investment limits as part of the TM strategy for 2014 in anticipation of "bail in".
24. Following advice from our advisors, Arlingclose, enquires on options for longer term deposits with covered bonds / Floating Rate Notes (FRN's) and similar instruments are ongoing with a view of investing up to our £30M limit for long term investments (currently £11M, plus commitment to invest another £7M in October) to optimise

investment income. These deals will generate around £125k in a full year and about £59k for 2014/15.

25. The Authority has internally managed investments amounting to £78.5M as at the end of September and the tables below show a breakdown by credit rating and maturity and summarises activity during the year: It also shows the new committed deals

	Balance on 01/04/2014	Investments Repaid	New Investments	Balance as at 30/9/2014	Increase/ (Decrease) in Investment for Year
	£M	£M	£M	£M	£M
Short Term Investments	18.3	(24.0)	18.0	12.3	(6.0)
Money Market Funds & Call Accounts	48.1	(207.0)	219.1	60.2	12.1
Bonds	3.0	0.0	3.0	6.0	3.0
Long Term Investments	0.0	0.0	0.0	0.0	0.0
<b>Total Investments</b>	<b>69.4</b>	<b>(231.0)</b>	<b>240.1</b>	<b>78.5</b>	<b>9.1</b>

<b>Current Investments</b>	<b>At 30th September 2014 £'000</b>	<b>Date of Maturity</b>	<b>Yield %</b>	<b>Rating</b>
Lloyds Bank Plc	2,000	15/12/2014	0.65	A
Lloyds Bank Plc	2,000	15/12/2014	0.57	A
Nationwide Building Society	5,000	15/12/2014	0.50	A
Nationwide Building Society	1,000	01/10/2014	0.74	A
Nationwide Building Society	1,000	15/10/2014	0.76	A
Nationwide Building Society	1,000	17/11/2014	0.78	A
Money Market Funds	23,967	Call	Average 0.41	A+ to AA-
Santander UK Plc	10,000	Call	0.80	A
Bank of Scotland Plc	2,951	Call	0.40	A
Svenska Handelsbanken – A SHS	4,401	Call	0.40	AA-
HSBC Bank PLC	9,093	Call	0.80	AA-
Barclays Bank PLC	9,790	Call	0.65	A
European Investment Bank - Bond	1,000	15/04/2025	5.27	AAA
European Investment Bank - Bond	1,000	07/06/2025	5.16	AAA
European Investment Bank - Bond	1,000	07/06/2025	5.49	AAA
Yorkshire Building Society Covered Bond	3,333	12/08/2018	2.034	AA+
<b>Committed Investments</b>				
Volkswagen	2,007	20/08/2015	1.00	A
Rabobank Nederland	2,062	10/09/2015	0.95	AA-
Leeds Building Society	3,005	01/10/2019	3m Libor +0.36%	AAA



### **Counterparty Update**

26. The European Parliament approved the EU *Bank Recovery and Resolution Directive (BRRD)* on April 15, 2014. Taking the view that potential extraordinary government support available to banks' senior unsecured bondholders will likely diminish within its two-year rating horizon for investment-grade entities, in April Standard & Poor's revised the Outlook of Barclays, Deutsche Bank, Credit Suisse and ING Bank from Stable to Negative (note, this is not the same as a rating review negative). In May, Moody's also changed the outlook from stable to negative for 82 European banks and from positive to stable for two European banks. The institutions affected on the Authority's lending list are Nationwide Building Society, Svenska Handelsbanken.
27. In August Moody's changed its outlook for the UK banking system from stable to negative, citing the reduction of government support for systemic banks as the reason. Although the agency believes that the stand-alone financial strength of UK institutions is improving they believed that this is more than offset by the potential bail-in risk now faced by investors. Similarly, in August S&P revised the outlooks for major Canadian banks to negative following the government's announcement of a potential bail-in policy framework.
28. Banks in the UK and EU face banks face stress tests this autumn, which may result in some institutions having to additionally bolster their capital buffers. The extent to which this might be required and the form they will have to take casts uncertainty over capital requirements in the system.
29. The UK is implementing the final bail-in provisions of the EU Bank Recovery and Resolution Directive to commence in January 2015, a year ahead of most other countries. Credit rating agencies have stated they plan to review EU banks' ratings in line with each country's implementation of the directive. Many UK banks, have standalone ratings in the "BBB" category, with uplifts for potential government support taking them into the "A" category. There is therefore a realistic risk that some major UK banks' credit ratings will fall below A- this financial year if this uplift is removed. We are not proposing to lower our counterparty to below A- to accommodate these banks but we may wish to continue investing in them through instant access as part of our non-specified investments. In order to accommodate this it is recommended that this limit be increased from the current level of £3M to £5M.

### **Authority Banking Arrangements**

30. As reported previously following the downgrading of the Co-op bank and the end of our contract with them, the Authority has moved its banking arrangements to Lloyds Bank from 1<sup>st</sup> October 2014 with a cross over period of 3 months up to the 31<sup>st</sup> December 2014 when all banking with Co-op will cease. Until this time we will continue to mitigate our exposure to credit risk as reported in the review of Prudential Limits and Treasury Management Outturn 2013/14 submitted to council on the 16 July and can be found as item 13 via the following link:  
<http://www.southampton.gov.uk/modernGov/ieListDocuments.aspx?CId=122&MId=2832&Ver=4>

## **BUDGETED INCOME AND EXPENDITURE**

### **Investments**

31. The Council does not expect any losses from non-performance in relation to its investments by any of its counterparties. The UK Bank Rate has been maintained at 0.5% since March 2009 and is not expected to rise this financial year. As a consequence short-term money market rates have remained at relatively low levels with new deposits being made at an average rate of 0.55%, investments in Money Market Funds and call accounts generated an average rate of 0.49%. Average cash balances were £102.5M during the quarter; these are expected to decline towards the end of the financial year as the incidence of government grant income and council tax income is skewed towards the earlier part of the year.
32. The Authority's budgeted investment income for the year was estimated at £0.3M, the Authority currently anticipates an investment outturn of £0.8M for the year based on current and committed deals. However following advice from our treasury advisors and our continued high investment balances the Authority has estimated it will have sufficient cash balances over the medium term to consider investing in further longer term financial instruments which will generate a better return.

### **Expenditure**

33. The interest cost of financing the Authority's long term and short term loan debt is charged corporately to the Income and Expenditure account. The interest cost in 2014/15 of financing the Authority's loan debt is currently expected to be £9.8M compared with an approved estimate of £11.2M, a saving of £1.4M, of which £0.8M relates to the HRA. This is mainly due to variable interest rates being lower than those estimated, no new long term borrowing being taken in 2013/14, slippage on the HRA capital programme to 2015/16 and deferring any new borrowing to later in the year.

## **COMPLIANCE WITH PRUDENTIAL INDICATORS**

34. All indicators to date complied with the Prudential Indicators approved by Council on 12 February 2014, item 87.

<http://www.southampton.gov.uk/modernGov/ieListDocuments.aspx?CId=122&MId=2469&Ver=4>

Details of the performance against key indicators and any proposed changes are shown below:

### **Capital Financing Requirement Gross and Actual External Debt**

35. The Capital Financing Requirement (CFR) measures the Council's underlying need to borrow for a capital purpose. In order to ensure that over the medium term net borrowing will only be for a capital purpose, the Council ensures that net external borrowing does not, except in the short term, exceed the CFR in the preceding year, plus the estimates of any additional capital financing requirement for the current and next two financial years. It differs from actual borrowing due to decisions taken to use internal balances and cash rather than borrow. The table below shows the actual position as at 31 March 2014 and the estimated position for the current and next two years based on the capital programme submitted to council on the 17 September 2014.

Capital Financing Requirement	2013/14 Actual £M	2014/15 Approved £M	2014/15 Forecast £M	2015/16 Revised Estimate £M	2016/17 Revised Estimate £M
<b>Balance B/F</b>	<b>433.2</b>	<b>430.2</b>	<b>425.0</b>	<b>431.0</b>	<b>438.9</b>
Capital expenditure financed from borrowing (inc PFI)					
General Fund (GF)	10.8	10.7	7.5	0.5	0.0
HRA	0.0	23.1	16.0	21.2	3.1
GF Temporary Funding (Repayment)	(5.8)	(3.4)	(3.7)	0.0	0.0
HRA Voluntary Repayment of Debt	(5.6)	(5.1)	(5.1)	(5.1)	(5.1)
GF Revenue provision for debt Redemption.	(4.5)	(6.9)	(6.2)	(6.0)	(5.9)
Movement in Other Long Term Liabilities	(3.1)	(2.4)	(2.5)	(2.7)	(3.1)
<b>Cumulative Maximum External Borrowing Requirement</b>	<b>425.0</b>	<b>446.2</b>	<b>431.0</b>	<b>438.9</b>	<b>427.9</b>

36. The Council reports that it has not borrowed in advance of need and that it has continued the use of internal resources in lieu of borrowing as this has been the most cost effective means of funding past capital expenditure to date. In the Prudential Code (November 2011), it states '*Where there is a significant difference between the net and gross borrowing position the risks and benefits associated with this strategy should be clearly stated in the annual strategy*'. The Council has had no difficulty in meeting this requirement so far in 2014/15, nor is there any difficulties envisaged for future years. This view takes into account current commitments, existing plans and the proposals in the approved budget.

	31/03/2014 Actual £M	31/03/2015 Approved £M	31/03/2015 Estimate £M	31/03/2016 Estimate £M	31/03/2017 Estimate £M
General Fund CFR	266.4	261.1	261.5	253.3	244.3
Housing CFR	158.6	185.1	169.5	185.6	183.6
<b>CFR</b>	<b>425.0</b>	<b>446.2</b>	<b>431.0</b>	<b>438.9</b>	<b>427.9</b>
Gross Long term Debt	342.0	351.0	335.0	349.0	370.0
<b>Difference</b>	<b>83.0</b>	<b>95.2</b>	<b>96.0</b>	<b>89.9</b>	<b>57.9</b>
Short Term Debt	10.0	10.0	20.0	30.0	40.0
<b>Difference</b>	<b>73.0</b>	<b>85.2</b>	<b>76.0</b>	<b>59.9</b>	<b>17.9</b>
Borrowing in excess of CFR? (Y/N)	<b>N</b>	<b>N</b>	<b>N</b>	<b>N</b>	<b>N</b>
<b>Investments</b>	<b>(69)</b>	<b>(43)</b>	<b>(53)</b>	<b>(53)</b>	<b>(53)</b>

### Authorised Limit and Operational Boundary for External Debt

37. The Local Government Act 2003 requires the Council to set an Affordable Borrowing Limit, irrespective of their indebted status. This is a statutory limit which should not be breached. The Council's **Affordable / Authorised Borrowing Limit** was set at £760M for 2014/15 (£674M for borrowing and £86M for other long term liabilities).
38. The **Operational Boundary** is based on the same estimates as the Authorised Limit but reflects the most likely, prudent but not worst case scenario without the

additional headroom included within the Authorised Limit. The Operational Boundary for 2014/15 was set at £750M (£672M for borrowing and £78M for other long term liabilities).

39. The above limits are set to allow maximum flexibility within TM, for example a full debt restructure. Actual borrowing as detailed in paragraph 11 is significantly below this and reflects decisions taken to use internal balances and cash rather than to physically borrow and shows the position at a point in time. No new borrowing is expected to take place until later in the financial year.
40. The Chief Financial Officer (CFO) confirms that there were no breaches to the Authorised Limit and the Operational Boundary and during the period to the end of September 2014, borrowing at its peak was £274M (other long term liabilities £78M) and there is no proposal to change these limits at this time.

**Upper Limits for Fixed and Variable Interest Rate Exposure**

41. These indicators allow the Council to manage the extent to which it is exposed to changes in interest rates. The upper limit for variable rate exposure allows for the use of variable rate debt to offset exposure to changes in short-term rates on our portfolio of investments.

	<b>Limits for 2014/15</b> %
Upper Limit for Fixed Rate Exposure	100
Compliance with Limits:	Yes
Upper Limit for Variable Rate Exposure	50
Compliance with Limits:	Yes

42. The Upper limit represents the maximum proportion of borrowing which is subject to variable rate interest and was set at 50%, although in practice it would be unusual for the exposure to exceed 25% based on past performance, the highest to date is 15.8%. The limit was set at a higher level to allow for a possible adverse cash flow position, leading to a need for increased borrowing on the temporary market and to take advantage of the low rates available through the PWLB for variable debt. There has been no adverse cash flow to date but it is proposed that the limit remain at 50%, to allow for flexibility in case of any slippage in expected capital receipts.

**Total principal sums invested for periods longer than 364 days**

43. This indicator allows the Council to manage the risk inherent in longer term investments; the limit for 2014/15 was set at £30M. As detailed in paragraph 24 we currently have £11M invested in long term instruments with commitment for another £7M during October.

**Liquidity**

44. The Council has adopted a voluntary measure of its exposure to liquidity risk by monitoring the amount of cash available within a rolling three month period with the view of looking to borrow short term if cash available in instant access accounts falls below £25M.

### **Maturity Structure of Fixed Rate Borrowing**

45. This indicator highlights the existence of any large concentrations of fixed rate debt needing to be replaced at times of uncertainty over interest rates and is designed to protect against excessive exposures to interest rate changes in any one period.

	Lower Limit	Upper Limit	Actual Fixed Debt as at 30/9/2014	Average Fixed Rate as at 30/9/2014	% of Fixed Rate as at 30/9/2014	Compliance with set Limits?
	%	%	£M	%		
Under 12 months	0	45	9.4	2.44	4.20	Yes
12 months and within 24 months	0	45	0.0	0.00	0.00	Yes
24 months and within 5 years	0	50	0.0	0.00	0.00	Yes
5 years and within 10 years	0	75	75.2	3.23	33.66	Yes
10 years and within 15 years	0	75	0.0	0.00	0.00	Yes
15 years and within 20 years	0	75	0.0	0.00	0.00	Yes
20 years and within 25 years	0	75	0.0	0.00	0.00	Yes
25 years and within 30 years	0	75	10.0	4.68	4.48	Yes
30 years and within 35 years	0	75	5.0	4.60	2.24	Yes
35 years and within 40 years	0	75	42.0	3.99	18.80	Yes
40 years and within 45 years	0	75	50.6	3.62	22.65	Yes
45 years and within 50 years	0	75	31.2	3.56	13.98	Yes
50 years and above	0	100	0.0	0.00	0.00	Yes
			<b>223.4</b>	<b>3.43</b>	<b>100.00</b>	

For this indicator, all of the Council LOBO loans are within the call period so the maturity date of the loans is treated as due in the year.

### **Credit Risk**

46. The Council confirms it considers security, liquidity and yield, in that order, when making investment decisions. Credit ratings remain an important element of assessing credit risk, but they are not the sole feature in the Council's assessment of counterparty credit risk. The Council also considers alternative assessments of credit strength, and information on corporate developments of and market sentiment towards counterparties. The following key tools are used to assess credit risk:

- Published credit ratings of the financial institution (minimum A- or equivalent) and its sovereign (minimum AA+ or equivalent for non-UK sovereigns);
- Sovereign support mechanisms;
- Credit default swaps (where quoted);
- Share prices (where available);
- Economic fundamentals, such as a country's net debt as a percentage of its GDP);
- Corporate developments, news, articles, markets sentiment and momentum;
- Corporate developments, news, articles, markets sentiment and momentum.

The Council can confirm that all investments were made in line with minimum credit rating criteria set in the 2014/15 TMSS.

### **Housing Revenue Account (HRA) Limit on Indebtedness**

47. Local authorities are required to report the level of the HRA CFR compared to the level of debt which was imposed by the CLG of self-financing at the time of implementation. The following tables show this plus the movement in year.

HRA Summary of Borrowing	2013/14 Actual £m	2014/15 Approved £m	2014/15 Estimate £m	2015/16 Estimate £m	2016/17 Estimate £m
Brought Forward	163.8	167.1	158.6	169.5	185.6
Maturing Debt	(5.6)	(5.1)	(5.1)	(5.1)	(5.1)
New borrowing	0.4	23.1	16.0	21.2	3.1
<b>Carried forward</b>	<b>158.6</b>	<b>185.1</b>	<b>169.5</b>	<b>185.6</b>	<b>183.6</b>
HRA Debt Cap (as prescribed by CLG)	199.6	199.6	199.6	199.6	199.6
Headroom	41.0	14.5	30.1	14.0	16.0

### **Ratio of Financing Costs to Net Revenue Stream**

48. This is an indicator of affordability and highlights the revenue implications of existing and proposed capital expenditure by identifying the proportion of the revenue budget required to meet borrowing costs. The definition of financing costs is set out at paragraph 87 of the Prudential Code. The ratio is based on costs net of investment income. The increase in the HRA financing costs is due to the reform of HRA of council housing finance which took effect from 28 March 2012. During 2013/14 the HRA made a voluntary debt repayment of £5.6M, which has led to an increase in the financing ratio for the year. This will result in lower borrowing costs for future years. The upper limit for this ratio is currently set at 10% for the General Fund to allow for known borrowing decision in the next two years and to allow for additional borrowing affecting major schemes.

Ratio of Financing Costs to Net Revenue Stream	2013/14 Actual %	2014/15 Approved %	2014/15 Forecast %	2015/16 Forecast %	2016/17 Forecast %
General Fund	6.95%	6.96%	5.97%	7.46%	8.58%
HRA	16.24%	16.33%	14.88%	15.75%	16.01%
<b>Total</b>	<b>10.28%</b>	<b>10.39%</b>	<b>9.27%</b>	<b>10.94%</b>	<b>12.19%</b>

### **SUMMARY**

49. In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of the treasury management activity up to the 30 September 2014. As indicated in this report none of the Prudential Indicators have been breached and a prudent approach has been taking in relation to investment activity with priority being given to security and liquidity over yield
50. In addition to the CIPFA's requirement to produce a mid and year end report, each quarter as part of corporate monitoring a summary of Treasury Management activity is prepared. This is presented to Cabinet as part of the Quarterly Revenue Financial Monitoring report.
51. For further information please see the following links:

*Treasury Management Strategy Statement for 2014 on 12 February 2014, item 87.*  
<http://www.southampton.gov.uk/modernGov/ieListDocuments.aspx?CId=122&MId=2469&Ver=4>

*Treasury Management Outturn Report on 16<sup>th</sup> July 2014, item 35.*  
<http://www.southampton.gov.uk/modernGov/ieListDocuments.aspx?CId=122&MId=2832&Ver=4>

*Quarterly Revenue Financial Monitoring report, item 23 (Appendix 11)*

## RESOURCE IMPLICATIONS

### Capital

52. The Capital implications were considered as part of the Capital Update report submitted to Council on the 17 September 2014.

### Revenue

53. The revenue implications are considered as part of ongoing monitoring which is reported to Cabinet each Quarter and as part of the budget setting process.

### Property/Other

54. None

## LEGAL IMPLICATIONS

### Statutory power to undertake proposals in the report:

55. Local Authority borrowing is regulated by Part 1, of the Local Government Act 2003, which introduced the new Prudential Capital Finance System. From 1 April 2004, investments are dealt with, not in secondary legislation, but through guidance. Similarly, there is guidance on prudent investment practice, issued by the Secretary of State under Section 15(1)(a) of the 2003 Act. A local authority has the power to invest for "any purpose relevant to its functions under any enactment or for the purposes of the prudent management of its financial affairs". The reference to the "prudent management of its financial affairs" is included to cover investments, which are not directly linked to identifiable statutory functions but are simply made in the course of treasury management.

This also allows the temporary investment of funds borrowed for the purpose of expenditure in the reasonably near future; however, the speculative procedure of borrowing purely in order to invest and make a return remains unlawful.

### Other Legal Implications:

56. None

## POLICY FRAMEWORK IMPLICATIONS

57. This report has been prepared in accordance with the CIPFA Code of Practice on TM.

KEY DECISION? No

WARDS/COMMUNITIES AFFECTED:	All
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## SUPPORTING DOCUMENTATION

### Appendices

1.	Economic performance to date and outlook for Q3 and Q4 2014/15
2.	Glossary of Treasury Terms

### Documents In Members' Rooms

1.	None
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### Equality Impact Assessment

Do the implications/subject of the report require an Equality Impact Assessment (EIA) to be carried out.	No
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### Other Background Documents

#### Equality Impact Assessment and Other Background documents available for inspection at:

Title of Background Paper(s)

Relevant Paragraph of the Access to Information Procedure Rules / Schedule 12A allowing document to be Exempt/Confidential (if applicable)

1.	<a href="#">TREASURY MANAGEMENT STRATEGY AND PRUDENTIAL LIMITS 2014/15 to 2016/17 – Council 12 February 2014</a>
2.	<a href="#">REVIEW OF PRUDENTIAL LIMITS AND TREASURY MANAGEMENT OUTURN 2013/14 – Council 16 July 2014</a>
3.	<a href="#">CORPORATE REVENUE FINANCIAL MONITORING FOR THE PERIOD TO THE END JUNE 2014– Cabinet 19 August 2014</a>



## 1. Economic Performance Q1 and Q2

**Growth and Inflation:** The recent strong performance of the UK economy continued with output growing at 0.8% in Q1 2014 and at 0.9% in Q2. The services sector once again grew strongly. On the back of strong consumption growth, business investment appeared to be recovering quickly, albeit from a low base. The annual CPI inflation rate fell to 1.5% year-on-year in August.

Revisions to the Gross Domestic Product (GDP) methodology, now compliant with the European System of Accounting 2010, mean that growth is now estimated to be 2.7% above its pre-recession peak in Q1 2008 rather than just 0.2% higher, the general theme being that the recession was not as deep and the recovery was earlier than initially estimated. In anticipation of these revisions, the MPC has forecast growth at 3.4% in 2014.

**Unemployment:** The labour market continued to improve, with strong employment gains and the headline unemployment rate falling to 6.2%. However, earnings growth remained very weak, rising just 0.6% for the three months May-July 2014 when compared to the same period a year earlier. The growth in employment was masked by a large number of zero-hour contracts and involuntary part-time working.

**UK Monetary Policy:** The Monetary Policy Committee (MPC) made no change to the Bank Rate of 0.5% and maintained asset purchases at £375bn. However, there was a marked shift in tone from the Bank of England's Governor and other MPC members. In his Mansion House speech in June Governor Mark Carney warned that interest rates might rise sooner than financial markets were expecting. Following some mixed messages from Governor Carney later in the summer, the minutes of the August and September MPC meetings revealed a split vote with regards to the Bank Rate. Ian McCafferty and Martin Weale voted to increase Bank Rate by 0.25%, arguing economic circumstances were sufficient to justify an immediate rise. The MPC emphasised that when Bank Rate did begin to rise, it was expected to do so only gradually and would likely remain below average historical levels for some time to come.

In the Bank of England's August Inflation Report the Bank forecast growth to be around 3½% in 2014, easing back thereafter to around its pre-crisis historical average rate. Inflation was forecast to remain at, or slightly below, 2% before reaching the target at the end of the 2-year forecast period.

The Bank's Financial Policy Committee also announced a range of measures to cool the UK's housing market to avert the potential of spiralling house prices derailing a sustainable economic recovery. Key recommendations included lenders stress-testing mortgage applicants can cope with a 3% rise in interest rates; putting a 15% cap on the number of mortgages at more than 4.5 times the borrower's income; and a separate Treasury pledge banning anyone applying for a loan through the Help to Buy scheme borrowing more than 4.5 times their income. The Prudential Regulation Authority also announced that it intends to consult on capital requirements for mortgages.

The result of the Scottish referendum in the end was close, but not as close as many believed it might be. However, the political upheaval set in motion (the Prime Minister's linking of a more devolved Scotland to giving greater powers to English MPs over English-only legislation, the prospect of Scotland's potential freedom to raise taxes not being

replicated elsewhere in the UK) is arguably likely to be just as problematic in the run-up to and beyond next year's general election.

Eurozone inflation continued to fall towards zero (HICP inflation registered just 0.3% in September), and there was mounting evidence that the already feeble recovery was losing pace. The unemployment rate remained stubbornly high at 11.5%. The European Central Bank lowered its official benchmark interest rate from 0.15% to 0.05%. The rate it pays on commercial bank balances held with it was also cut further into negative territory from -0.1% to -0.2% and the Marginal Lending Facility rate cut further to 0.3%. The ECB also announced a programme of acquiring Asset Backed Securities (ABS) from banks in an effort to encourage lending which was viewed as being one step away from full blown Quantitative Easing (QE) adopted by the US, UK and Japanese central banks. The minutes of the Bank of England's MPC meeting in September noted that "*weakness in the euro area had been the most significant development during the month*" and that, if it led once again to uncertainty about the sustainability of euro-area public and external debt, it could damage confidence and disrupt financial markets.

There was no change from the US Federal Reserve as the central bank kept policy on its current track with a reduction in asset purchases by \$10 billion per month. Asset purchases are expected to end by October 2014, expectations therefore turned towards the timing of rate increases. The US economy rebounded strongly in Q2 with annualised growth of 4.6%.

**Market reaction:** Gilt yields have continued to decline and hit a financial year low at the end of August, before ticking upwards in the run up to the Scottish referendum. What has driven yields lower is a combination of factors but the primary drivers have been the escalation of geo-political risk within the Middle East and Ukraine alongside the slide towards deflation within the Eurozone (EZ).

## 2. Outlook for Q3 and Q4

The stronger economic growth seen in the UK over the past six months is likely to use up spare capacity more quickly than previously assumed. Arlingclose has brought forward the timing for the first rise in Bank Rate to Q3 2015.

In addition to two MPC members having voted for a rate rise in August and September, the rhetoric from Committee members has in general become more hawkish. However, the lack of inflationary pressure is expected to allow policymakers to hold off monetary tightening for longer than the market currently expects. The near-term risk is that the Bank Rate could rise sooner than anticipated, which is captured in the 'upside risk' range of our forecast table below.

The focus is now on the rate of increase and the medium-term peak and, in this respect, expectations are that rates will rise slowly and to a lower level than in the past.

	Dec-14	Mar-15	Jun-15	Sep-15	Dec-15	Mar-16	Jun-16	Sep-16	Dec-16	Mar-17	Jun-17
Official Bank Rate											
Upside risk	0.25	0.25	0.25	0.25	0.25	0.25	0.50	0.50	0.50	0.50	0.50
Arlingclose Central Case	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50
Downside risk				0.25	0.25	0.50	0.50	0.75	0.75	1.00	1.00

### GLOSSARY OF TREASURY TERMS

**Authorised Limit (Also known as the Affordable Limit):**

A statutory limit that sets the maximum level of external borrowing on a gross basis (i.e. not net of investments) for the Council. It is measured on a daily basis against all external borrowing items on the Balance Sheet (i.e. long and short term borrowing, overdrawn bank balances and long term liabilities).

**Balances and Reserves:**

Accumulated sums that are maintained either earmarked for specific future costs or commitments or generally held to meet unforeseen or emergency expenditure.

**Bank Rate:**

The official interest rate set by the Bank of England's Monetary Policy Committee and what is generally termed at the "base rate". This rate is also referred to as the 'repo rate'.

**Basis Point:**

A unit of measure used in finance to describe the percentage change in the value or rate of a financial instrument. One basis point is equivalent to 0.01% (1/100th of a percent). In most cases, it refers to changes in **interest rates** and **bond yields**. For example, if interest rates rise by 25 basis points, it means that rates have risen by 0.25% percentage points. If rates were at 2.50%, and rose by 0.25%, or 25 basis points, the new interest rate would be 2.75%. In the bond market, a basis point is used to refer to the yield that a bond pays to the investor. For example, if a bond yield moves from 5.45% to 5.65%, it is said to have risen by 20 basis points. The usage of the basis point measure is primarily used in respect to yields and interest rates, but it may also be used to refer to the percentage change in the value of an asset such as a stock.

**Bond:**

A certificate of debt issued by a company, government, or other institution. The bond holder receives interest at a rate stated at the time of issue of the bond. The price of a bond may vary during its life.

**Capital Expenditure:**

Expenditure on the acquisition, creation or enhancement of capital assets.

**Capital Financing Requirement (CFR):**

The CFR is simply the total historic outstanding capital expenditure which has not yet been paid for from either revenue or capital resources. It is essentially a measure of the Council's underlying borrowing need.

**Capital Receipts:**

Money obtained on the sale of a capital asset.

**CD's:**

Certificates of Deposits with banks and building societies

**Comprehensive Spending Review (CSR):**

Comprehensive Spending Review is a governmental process in the United Kingdom carried out by **HM Treasury** to set firm expenditure limits and, through public service agreements, define the key improvements that the public can expect from these resources. Spending Reviews typically focus upon one or several aspects of public spending while the CSR focuses upon each government department's spending requirements from a zero base (i.e. without reference to past plans or, initially, current expenditure).

**Constant Net Asset Value (CNAV)**

These are Money Market Funds which maintain a stable price of £1 per share when investors redeem or purchase shares which mean that that any investment will not fluctuate in value.

**Corporate Bonds:**

Corporate bonds are bonds issued by companies. The term is often used to cover all bonds other than those issued by governments in their own currencies and includes issues by companies, supranational organisations and government agencies.

**Cost of Carry:**

The "cost of carry" is the difference between what is paid to borrow compared to the interest which could be earned. For example, if one takes out borrowing at 5% and invests the money at 1.5%, there is a cost of carry of 3.5%.

**Counterparty List:**

List of approved financial institutions with which the Council can place investments with.

**Covered Bond:**

Covered bonds are debt securities backed by cash flows from mortgages or public sector loans. They are similar in many ways to asset-backed securities created in securitisation, but covered bond assets remain on the issuer's consolidated balance sheet (usually with an appropriate capital charge). The covered bonds continue as obligations of the issuer (often a bank); in essence, the investor has recourse against the issuer and the collateral, sometimes known as "dual recourse."

**CPI :**

Consumer Price Index – the UK's main measure of inflation.

**Credit Rating:**

Formal opinion by a registered rating agency of a counterparty's future ability to meet its financial liabilities; these are opinions only and not guarantees.

**Department for Communities and Local Government (DCLG) :**

The DCLG is the UK Government department for Communities and Local Government in England. It was established in May 2006 and is the successor to the Office of the Deputy Prime Minister, established in 2001.

**Debt Management Office (DMO):**

The DMO is an Executive Agency of Her Majesty's Treasury and provides direct access for local authorities into a government deposit facility known as the **DMADF**. All deposits are guaranteed by HM Government and therefore have the equivalent of a sovereign triple-A

credit rating.

**Diversification /diversified exposure:**

The spreading of investments among different types of assets or between markets in order to reduce risk.

**Federal Reserve:**

The US central bank. (Often referred to as “the Fed”).

**Floating rate notes (FRNs) :**

These are bonds that have a variable coupon, equal to a money market reference rate, like LIBOR or federal funds rate, plus a quoted spread (a.k.a. quoted margin). The spread is a rate that remains constant. Almost all FRNs have quarterly coupons, i.e. they pay out interest every three months. At the beginning of each coupon period, the coupon is calculated by taking the fixing of the reference rate for that day and adding the spread. A typical coupon would look like 3 months USD LIBOR +0.20%.

**FTSE 100 Index:**

The FTSE 100 Index is a share index of the 100 companies listed on the London Stock Exchange with the highest market capitalisation. It is one of the most widely used stock indices and is seen as a gauge of business prosperity for business regulated by UK company law. The index is maintained by the FTSE Group, a subsidiary of the London Stock Exchange Group.

**General Fund:**

This includes most of the day-to-day spending and income.

**Gilts:**

Gilts are bonds issued by the UK Government. They take their name from ‘gilt-edged’: being issued by the UK government, they are deemed to be very secure as the investor expects to receive the full face value of the bond to be repaid on maturity.

**Gross Domestic Product (GDP):**

Gross Domestic Product measures the value of goods and services produced within a country. GDP is the most comprehensive overall measure of economic output and provides key insight as to the driving forces of the economy.

**The G7:**

The G7, is a group consisting of the finance ministers of seven industrialised nations: namely the US, UK, France, Germany, Italy, Canada and Japan. They are seven of the eight (China excluded) wealthiest nations on Earth, not by GDP but by global net wealth. The G7 represents more than the 66% of net global wealth (\$223 trillion), according to Credit Suisse Global Wealth Report September 2012.

**IFRS:**

International Financial Reporting Standards.

**International Labour Organisation (ILO):**

The ILO Unemployment Rate refers to the percentage of economically active people who are unemployed by ILO standard and replaced the Claimant Unemployment Rate as the international standard for unemployment measurement in the UK.. Under the ILO approach,

those who are considered as unemployed are either out of work but are actively looking for a job or out of work and are waiting to start a new job in the next two weeks. ILO Unemployment Rate is measured by a monthly survey, which is called the Labour Force Survey in United Kingdom. Approximately 40,000 individuals are interviewed each month, and the unemployment figure reported is the average data for the previous three months.

**LIBID:**

The London Interbank Bid Rate (LIBID) is the rate bid by banks on Eurocurrency deposits (i.e. the rate at which a bank is willing to borrow from other banks). It is "the opposite" of the LIBOR (an offered, hence "ask" rate, the rate at which a bank will lend). Whilst the British Bankers' Association set LIBOR rates, there is no correspondent official LIBID fixing.

**LIBOR:**

The London Interbank Offered Rate (LIBOR) is the rate of interest that banks charge to lend money to each other. The British Bankers' Association (BBA) work with a small group of large banks to set the LIBOR rate each day. The wholesale markets allow banks who need money to be more fluid in the marketplace to borrow from those with surplus amounts. The banks with surplus amounts of money are keen to lend so that they can generate interest which it would not otherwise receive.

**LOBO:**

Stands for Lender Option Borrower Option. The underlying loan facility is typically very long-term - for example 40 to 60 years - and the interest rate is fixed. However, in the LOBO facility the lender has the option to call on the facilities at pre-determined future dates. On these call dates, the lender can propose or impose a new fixed rate for the remaining term of the facility and the borrower has the 'option' to either accept the new imposed fixed rate or repay the loan facility. The upshot of this is that on the option exercise date, the lender could propose an extreme fixed rate, say 20 per cent, which would effectively force the repayment of the underlying facility. The borrower's so called 'option' is only the inalienable right to accept or refuse a new deal such as a fixed rate of 20 per cent.

**Maturity:**

The date when an investment or borrowing is repaid.

**Maturity Structure / Profile:**

A table or graph showing the amount (or percentage) of debt or investments maturing over a time period. The amount or percent maturing could be shown on a year-by-year or quarter-by-quarter or month-by-month basis.

**Minimum Revenue Provision (MRP):**

An annual provision that the Council is statutorily required to set aside and charge to the Revenue Account for the repayment of debt associated with expenditure incurred on capital assets.

**Money Market Funds (MMF):**

Pooled funds which invest in a range of short term assets providing high credit quality and high liquidity.

**Multilateral Development Banks:**

See Supranational Bonds below.

**Non Specified Investment:**

Investments which fall outside the CLG Guidance for **Specified investments** (below).

**Operational Boundary:**

This linked directly to the Council's estimates of the CFR and estimates of other day to day cash flow requirements. This indicator is based on the same estimates as the Authorised Limit reflecting the most likely prudent but not worst case scenario but without the additional headroom included within the Authorised Limit.

**Premiums and Discounts:**

In the context of local authority borrowing,

- (a) the premium is the penalty arising when a loan is redeemed prior to its maturity date and
- (b) the discount is the gain arising when a loan is redeemed prior to its maturity date.

If on a £1 million loan, it is calculated that a £150,000 premium is payable on premature redemption, then the amount paid by the borrower to redeem the loan is £1,150,000 plus accrued interest. If on a £1 million loan, it is calculated\* that a £50,000 discount receivable on premature redemption, then the amount paid by the borrower to redeem the loan is £950,000 plus accrued interest. PWLB premium/discount rates are calculated according to the length of time to maturity, current market rates (plus a margin), and the existing loan rate which then produces a premium/discount dependent on whether the discount rate is lower/higher than the coupon rate.

*\*The calculation of the total amount payable to redeem a loan borrowed from the Public Works Loans Board (PWLB) is the present value of the remaining payments of principal and interest due in respect of the loan being repaid prematurely, calculated on normal actuarial principles. More details are contained in the PWLB's lending arrangements circular.*

**Prudential Code:**

Developed by CIPFA and introduced on 01/4/2004 as a professional code of practice to support local authority capital investment planning within a clear, affordable, prudent and sustainable framework and in accordance with good professional practice.

**Prudential Indicators:**

Indicators determined by the local authority to define its capital expenditure and asset management framework. They are designed to support and record local decision making in a manner that is publicly accountable; they are not intended to be comparative performance indicators

**Public Works Loans Board (PWLB):**

This is a statutory body operating within the United Kingdom Debt Management Office, an Executive Agency of HM Treasury. The PWLB's function is to lend money from the National Loans Fund to local authorities and other prescribed bodies, and to collect the repayments.

**Quantitative Easing (QE):**

In relation to the UK, it is the process used by the Bank of England to directly increase the quantity of money in the economy. It *“does not involve printing more banknotes. Instead, the Bank buys assets from private sector institutions – that could be insurance companies, pension funds, banks or non-financial firms – and credits the seller's bank account. So the seller has more money in their bank account, while their bank holds a corresponding claim against the Bank of England (known as reserves). The end result is more money out in the*

*wider economy*". Source: Bank of England.

**Repo Rate:**

The interest rate at which the central bank in a country repurchases government securities (such as Treasury securities) from commercial banks. The central bank raises the repo rate when it wishes to reduce the money supply in the short term, while it lowers the rate when it wishes to increase the money supply and stimulate growth.

**Revenue Expenditure:**

Expenditure to meet the continuing cost of delivery of services including salaries and wages, the purchase of materials and capital financing charges.

**RPI:**

Retail Prices Index is a monthly index demonstrating the movement in the cost of living as it tracks the prices of goods and services including mortgage interest and rent. Pensions and index-linked gilts are uprated using the RPI index.

**(Short) Term Deposits:**

Deposits of cash with terms attached relating to maturity and rate of return (Interest).

**Specified Investments:**

Term used in the CLG Guidance and Welsh Assembly Guidance for Local Authority Investments. Investments that offer high security and high liquidity, in sterling and for no more than one year. UK government, local authorities and bodies that have a high credit rating.

**Supported Borrowing:**

Borrowing for which the costs are supported by the government or third party.

**Supranational Bonds:**

Instruments issued by supranational organisations created by governments through international treaties (often called **multilateral development banks**). The bonds carry a AAA rating in their own right. Examples of supranational organisations are the European Investment Bank, the International Bank for Reconstruction and Development.

**T-Bills:**

Treasury Bills are short term Government debt instruments and, just like temporary loans used by local authorities, are a means to manage cash flow. Treasury Bills (T-Bills) are issued by the Debt Management Office and are an eligible sovereign instrument, meaning that they have a AAA-rating.

**Temporary Borrowing:**

Borrowing to cover peaks and troughs of cash flow, not to fund capital spending.

**Treasury Management Code:**

CIPFA's Code of Practice for Treasury Management in the Public Services, initially brought in 2003, subsequently updated in 2009 and 2011.

**Treasury Management Practices (TMP):**

Treasury Management Practices set out the manner in which the Council will seek to achieve its policies and objectives and prescribe how it will manage and control these



activities.

**Unsupported Borrowing:**

Borrowing which is self-financed by the local authority. This is also sometimes referred to as Prudential Borrowing.

**Variable Net Asset Value (VNAV):**

Redemptions and investments in Money Market Funds (MMF's) are on the basis of the fund's Net Asset Value (NAV) per share. The NAV of any money market fund is the market value of the fund's assets minus its liabilities and is stated on a per share basis. The net value of the assets held by an MMF can fluctuate, and the market value of a share may not always be exactly the amount that has been invested.

**Yield:**

The measure of the return on an investment instrument.

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