DECISION-MAKER:		GOVERNANCE COMMITTEE		
SUBJECT:		REVIEW OF PRUDENTIAL LIMITS AND TREASURY MANAGEMENT OUTTURN 2021/22		
DATE OF DECISION:		25 JULY 2022		
REPORT OF:		**EXECUTIVE DIRECTOR FINANCE & COMMERCIALISATION (S151 Officer)**		
CONTACT DETAILS				
Executive Directo	**Title:**	**Executive Director for Finance, Commercialisation & S151 Officer**		
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STATEMENT OF CONFIDENTIALITY		
NOT APPLICABLE		
BRIEF SUMMARY		
The purpose of this report is to inform Governance Committee of the Treasury Management activities and performance for 2021/22 against the approved Prudential Indicators for External Debt and Treasury Management.		
RECOMMENDATIONS:		
It is recommended that Governance committee:		
	(i)	Notes the Treasury Management (TM) activities for 2021/22 and the outturn on the Prudential Indicators.
	(ii)	Notes that the continued proactive approach to TM has led to reductions in borrowing costs and safeguarded investment income during the year.
REASONS FOR REPORT RECOMMENDATIONS		
1.	The reporting of the outturn position for 2021/22 forms part of the approval of the statutory accounts. The Treasury Management (TM) Strategy and Prudential Indicators are approved by Governance Committee in February each year in accordance with legislation and the Chartered Institute of Public Finance & Accountancy (CIPFA) Code of Practice.	
2. .	The Treasury Management 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 Governance Committee 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		

3.	No alternative options are relevant to this report.	
DETAIL (Including consultation carried out)		
CONSULTATION		
4.	Not applicable.	
BACKGROUND		
5.	The Local Government Act 2003 introduced a system for borrowing based largely on self-regulation by local authorities themselves. The basic principle of the new system is that local authorities will be free to borrow as long as their capital spending plans are affordable, prudent and sustainable.	
6.	CIPFA published a revised Prudential Code for Capital Finance and Treasury Management Code on 20th December 2021. The key changes in the two codes are around permitted reasons to borrow, knowledge and skills, and the management of non-treasury investments. Whilst the principles of the Prudential Code took immediate effect, local authorities were given the option to defer introducing the revised reporting requirements until the 2023/24 financial year. Due to the timing of the revised code, there was limited time to do a comprehensive review to fit in with our committee cycle, so it was decided to defer until next year. We will be assessing the new requirements during 2022/23 and will introduce changes as appropriate.	
7.	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 a year (mid-year and at year end).	
8.	The Authority's TM Strategy for 2021/22 was approved by Governance Committee on 15 February 2021. These were subsequently reviewed and revised as part of the Council's TM Strategy Statement for 2022/23 at Governance Committee on 14 February 2022. The 2017 Prudential Code includes a requirement for local authorities to provide a Capital Strategy, a summary document approved by full Council covering capital expenditure and financing, treasury management and non-treasury investments. The Authority's Capital Strategy, complying with CIPFA's requirement, was approved by full Council on 23 February 2022.	
9.	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 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.	
10.	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 the outturn position on treasury management transactions in 2021/22; and
	e)	confirms compliance with treasury limits and Prudential Indicators.
11.	The report and appendices highlight that:	
	a)	Borrowing activities have been undertaken within the borrowing limits approved by Governance Committee on 15 February 2021 and reviewed on 14 February 2022.
	b)	There has been full compliance with the Prudential Indicators approved by Governance Committee on 15 February 2021 and reviewed on 14 February 2022.
	c)	As we have an increasing borrowing requirement our overall treasury strategy is to minimise both external borrowing and investments and to only borrow to the level of its net borrowing requirement. The reasons for this are to reduce credit risk, take pressure off the Council's lending list and also to avoid the cost of carry existing in the current interest rate environment. Throughout the year, capital expenditure levels, market conditions and interest rate levels were monitored to minimise borrowing costs over the medium to longer term and to maintain stability.
	d)	CIPFA published a revised Treasury Management in the Public Services Code of Practice and Cross-Sectoral Guidance Notes on 20th December 2021. These define treasury management investments as investments that arise from the organisation's cash flows or treasury risk management activity that ultimately represents balances that need to be invested until the cash is required for use in the course of business. As reported previously SCC holds £27M in the CCLA property fund which was reviewed following the revised CIPFA guidance, and it still meets our medium term investments objectives whilst interest earned is above current PWLB 2O year maturity rates. This will remain under review in conjunction with our financial advisors. For further details on the funds performance see Appendix 2, paragraphs 32 to 35.
	e)	Total investment returns during 2021/22 were £1.1M at an average rate of 3.46%.
	f)	The differential between debt costs and investment earnings continued to be acute, resulting in the use of internal resources in lieu of borrowing often being the most cost effective means of financing capital expenditure. As a result, the average rate for repayment of debt, (the Consolidated Loans & Investment Account Rate – CLIA), at 2.80%, is lower than that budgeted but higher than last year (2.75%), this is mainly as a result of maturing short term debt which was not replaced due to high cash flows. It is the intention to borrow in the short term markets during 2022/23 to take further advantage of the current interest environment.
	g)	Since 2012, the Council has pursued a strategy of internal borrowing – minimising external borrowing by running down its own investment balances and only borrowing short term to cover cash flow

		requirements. This has both reduced the credit risk exposure and saved the Council money in terms of net interest costs.
	h)	In achieving interest rate savings the Council is exposed to interest rate risk by taking out variable debt. This was and continues to be very financially favourable in current markets but does mean that close monitoring of the markets is required to ensure that the Council can act quickly should the situation begin to change, for example, during the year we borrowed £33M to introduce some certainty into the loan portfolio in a rising interest environment.
	i)	Net loan debt decreased during 2021/22 from £246M to £209M (£37M) as detailed in Appendix 2, paragraph 5. Actual debt charges for the year for borrowing (excluding HCC transferred debt and PFI schemes) was £7.0M at an average interest rate of 2.86%
	j)	The continuing economic recovery from the COVID-19 pandemic, together with the war in Ukraine, higher inflation, and higher interest rates were major issues over the period. This is expected to continue during the current financial year and will be monitored and reported as part of the quarterly monitoring and mid-year reports.
	k)	The impact of the COVID-19 pandemic continued in 2021/22 and central Government continued to assist cash flow by providing up front funding as far as possible, both in terms of the grants to businesses administered by the Council on its behalf and the funding to the local authority itself (under the business rates retention scheme). As a result of this grant funding year end investment balances were higher than expected and borrowing lower.
12.	Appendix 1 summarises the economic outlook and events in the context of which the Council operated its treasury function during 2021/22.	
13.	Appendix 2 summarises treasury activity during the year and covers: • Borrowing Requirement and Debt Management • Investment Activity • Non – Treasury Investments	
COMPLIANCE WITH PRUDENTIAL INDICATORS		
14.	It can be confirmed that the Council has complied with its Prudential Indicators for 2021/22, approved by Governance Committee on 15 February 2021 and reviewed on 14 February 2022.	
15.	In compliance with the requirements of the CIPFA Code of Practice this report provides members with a summary report of TM activity during 2021/22. None of the Prudential Indicators has been breached and a prudent approach has been taken in relation to investment activity with priority being given to security and liquidity over yield. The table below summarises the Key Indicators, further details can be seen in appendix 4.	

16. ***Table1: Key Prudential Indicators***

Indicator	Limit	Actual at 31/3/2022
Authorised Limit for external debt	£805M	£316M
Operational Limit for external debt	£705M	£316M
Maximum external borrowing year to date	£640M	£259M
Limit of fixed interest debt	100%	83%
Limit of variable interest debt	50%	17%
Limit for long term investments	£100M	£28M

OTHER

17. IFRS 16: The implementation of the new IFRS 16 Leases accounting standard was due to come into for force for local authorities from 1st April 2022. Following a consultation CIFPA/LASAAC announced an optional two year delay to the implementation of this standard a decision which was confirmed by the Financial Reporting Advisory Board in early April 2022. Therefore, no accounting changes have been made from 1st April 2022 and any proposed changes will be reported as part of the mid-year report.

RESOURCE IMPLICATIONS

Capital/Revenue

18. This report is a requirement of the TM Strategy, which was approved at Council on 14 February 2022.

19. The capital and revenue implications are considered as part of the outturn report that was presented to Cabinet on 18 July 2022.

20. 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 of financing the Authority's loan debt amounted to £7.21M in 2021/22. This is lower than budgeted mainly due to variable interest rates being lower than those estimated and minimal new long term borrowing being taken at preferential rates.

21. In addition, interest earned on temporary balances invested externally is credited to the Income and Expenditure account. In 2021/22 £1.4M was earned which was slightly higher than budgeted £1.3M mainly due to higher than expected balances.

22. The expenses of managing the Authority's loan debt consist of brokerage and internal administration charges. These are pooled and borne by the HRA and General Fund proportionately to the related loan debt. Debt management expenses amounted to £0.16M in 2021/22.

Property/Other

23. There are no specific property implications arising from this report.

LEGAL IMPLICATIONS	
Statutory power to undertake proposals in the report:	
24.	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:	
25.	None.
RISK MANAGEMENT IMPLICATIONS	
26.	Not Applicable
POLICY FRAMEWORK IMPLICATIONS	
27.	Not applicable. This report has been prepared in accordance with the CIPFA Code of Practice on TM.

KEY DECISION?	~~Yes~~/No
WARDS/COMMUNITIES AFFECTED:	NONE

SUPPORTING DOCUMENTATION	
Appendices	
1.	2021/22 Economic Background
2.	Treasury Activity during 2021/22
3.	Southampton Benchmarking 31st March 2022
4.	Compliance with Prudential Indicators
5.	Glossary of Treasury Terms
Documents In Members' Rooms	
1.	None.
Equality Impact Assessment	
Do the implications/subject of the report require an Equality and Safety Impact Assessments (ESIA) to be carried out.	**~~Yes~~/No**
Privacy Impact Assessment	
Do the implications/subject of the report require a Privacy Impact Assessment (PIA) to be carried out.	**~~Yes~~/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.	The Medium Term Financial Strategy, Budget Capital Programme 2021/22 to 2026/27 – reported to Council 23 February 2022	