

# Public Document Pack



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Our ref: Extra Governance & Audit Committee/Agenda  
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## GOVERNANCE AND AUDIT COMMITTEE

30 JULY 2014

An extraordinary meeting of the Governance and Audit Committee will be held at **2.00 pm on Wednesday, 30 July 2014** in the Austen Room, Council Offices, Cecil Street, Margate, Kent.

### Membership:

Councillor Worrow (Chairman); Councillors: Lodge-Pritchard (Vice-Chairman), Binks, Campbell, Day, Gibson, D Saunders, W Scobie and S Tomlinson

## AGENDA

Item  
No

Subject

1. **APOLOGIES FOR ABSENCE**

2. **DECLARATIONS OF INTEREST**

'To receive any declarations of interest. Members are advised to consider the advice contained within the Declaration of Interest Form attached at the back of this Agenda. If a Member declares an interest, they should complete that form and hand it to the Officer clerking the meeting and then take the prescribed course of action.

3. **CREDIT METHODOLOGY CHANGES** (Pages 1 - 8)

**Declaration of Interests Form**

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## CREDIT METHODOLOGY CHANGES

To: **Extraordinary Governance and Audit Committee – 30 July 2014**

Main Portfolio Area: **Finance**

By: **Capital & Treasury Finance Officer**

Classification: **Unrestricted**

Report Produced on: **25 June 2014**

Ward: **Thanet Wide**

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**Summary:** **This report concerns credit methodology changes and consequent changes to the Council's investment criteria.**

### For Decision

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#### **1.0 Introduction and Background**

1.1 In the Council's Treasury Management Strategy Statement, Minimum Revenue Provision Policy Statement and Annual Investment Strategy for 2014/15 (TMSS), minimum credit ratings criteria are set for investment counterparties.

1.2 Capita Asset Services (Capita), the Council's external treasury management advisor, has informed the Council of the following:

- The main ratings agencies (Fitch, Moody's and Standard & Poors) have provided some institutions with a rating uplift due to implied levels of sovereign support.
- Due to the evolving regulatory regime, it is expected that implied sovereign support levels are going to be removed and this process will commence this year.
- Capita is looking to pre-empt this process by making changes to its rating assessment methodology from 27 June 2014.

1.3 The current Capita methodology includes an assessment of the 'standalone' credit ratings provided by Fitch (Viability rating) and Moody's (Financial Strength rating). Due to the removal of sovereign support from agency ratings, Capita has reported that Fitch and Moodys' have suggested that their Viability and Financial Strength ratings respectively will become the same as their Long Term ratings.

1.4 The current Capita methodology also includes an assessment of the Fitch Support rating. Capita has reported that Fitch has begun assessing its Support ratings, with the expectation that these will be lowered to 5 which is defined as '*a bank for which there is a possibility of external support, but it cannot be relied upon.*' Capita has reported that all institutions are likely to drop to this level and hence there is little or no differentiation to be had by Capita continuing to assess Support ratings in its methodology.

1.5 Accordingly, the credit element of Capita's new rating assessment methodology will focus solely on the Short Term and Long Term ratings of an institution.

## **2.0 The Current Situation**

2.1 The Council's minimum credit ratings criteria for banks as set out in section 4.2 of its TMSS include Viability bb- (Fitch), Financial Strength C- (Moody's), and Support 3 (Fitch).

## **3.0 Options**

3.1 That the Governance and Audit Committee recommends to Cabinet that minimum credit ratings criteria for Viability, Financial Strength and Support no longer be included in the Council's TMSS. The relevant extract (section 4.2) of the TMSS is shown in Annex 1. There will be one Medium Quality category, instead of two, with a money limit of £5m.

3.2 That the Governance and Audit Committee recommends to Cabinet that the Council's TMSS remains unchanged.

## **4.0 Corporate Implications**

### **4.1 Financial and VAT**

5.1.1 If option 3.2 is chosen there is an expectation of a reduction in the Council's counterparty list in due course.

## **5.2 Legal**

5.2.1 This report evidences that the requirements of the CIPFA Code of Practice on Treasury Management continue to be met.

## **5.3 Corporate**

5.3.1 This report evidences that the Council continues to carefully manage its treasury function.

## **5.4 Equity and Equalities**

5.4.1 There are no equality or equity issues arising directly from this report.

## **6.0 Recommendation**

6.1 That the Governance and Audit Committee approves option 3.1 (in line with Capita's new rating assessment methodology) and recommends it to both Cabinet and Council.

## **7.0 Decision Making Process**

7.1 This report is to go to Cabinet and then Council for approval. The next Cabinet meeting is on 31 July 2014.

## **8.0 Disclaimer**

8.1 This report is a technical document focussing on public sector investments and borrowings and, as such, readers should not use the information contained within the report to inform personal investment or borrowing decisions. Neither Thanet District

Council nor any of its officers or employees makes any representation or warranty, express or implied, as to the accuracy or completeness of the information contained herein (such information being subject to change without notice) and shall not be in any way responsible or liable for the contents hereof and no reliance should be placed on the accuracy, fairness or completeness of the information contained in this document. Any opinions, forecasts or estimates herein constitute a judgement and there can be no assurance that they will be consistent with future results or events. No person accepts any liability whatsoever for any loss howsoever arising from any use of this document or its contents or otherwise in connection therewith.

Contact Officer:	Paul Cook, Interim Director of Corporate Resources extn 7617
Reporting to:	Sue McGonigal, Chief Executive and S151 Officer

### **Annex List**

Annex 1	Section 4.2 of the Council's TMSS
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### **Corporate Consultation Undertaken**

Finance	N/A
Legal	N/A

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**Annex 1**

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**SECTION 4.2 OF TREASURY MANAGEMENT STRATEGY STATEMENT,  
MINIMUM REVENUE PROVISION POLICY STATEMENT AND ANNUAL  
INVESTMENT STRATEGY FOR 2014/15**

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**4.2 Creditworthiness policy**

The primary principle governing the Council's investment criteria is the security of its investments, although the yield or return on the investment is also a key consideration. After this main principle, the Council will ensure that:

- It maintains a policy covering both the categories of investment types it will invest in, criteria for choosing investment counterparties with adequate security, and monitoring their security. This is set out in the specified and non-specified investment sections below; and
- It has sufficient liquidity in its investments. For this purpose it will set out procedures for determining the maximum periods for which funds may prudently be committed. These procedures also apply to the Council's prudential indicators covering the maximum principal sums invested.

The Section 151 Officer will maintain a counterparty list in compliance with the following criteria and will revise the criteria and submit them to Council for approval as necessary. These criteria are separate to that which determines which types of investment instrument are either specified or non-specified as it provides an overall pool of counterparties considered high quality which the Council may use, rather than defining what types of investment instruments are to be used.

The minimum rating criteria uses the lowest common denominator method of selecting counterparties and applying limits. This means that the application of the Council's minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by two agencies, one meets the Council's criteria, the other does not, the institution will fall outside the lending criteria. Credit rating information is supplied by Capita Asset Services our treasury consultants, on all active counterparties that comply with the criteria below. Any counterparty failing to meet the criteria would be omitted from the counterparty (dealing) list. Any rating changes, rating watches (notification of a likely change), rating outlooks (notification of a possible longer term change) are provided to officers almost immediately after they occur and this information is considered before dealing. For instance, a negative rating watch applying to a counterparty at the minimum Council criteria may be suspended from use, with all others being reviewed in light of market conditions.

The criteria for providing a pool of high quality investment counterparties (both specified and non-specified investments) is:

- Banks 1 - good credit quality – the Council will only use banks which:
  - i. are UK banks; and/or
  - ii. are non-UK and domiciled in a country which has a minimum sovereign long term rating of AAA

and have, as a minimum, the following Fitch, Moody's and Standard and Poors credit ratings (where rated):

- i. Short term – F1
- ii. Long term – A

- Banks 2 – Guaranteed Banks with suitable Sovereign Support – In addition, the Council will use banks whose ratings fall below the criteria specified above if all the following conditions are met:

- i. wholesale deposits in the bank are covered by a government guarantee;
- ii. the government providing the guarantee is the UK government or is rated AAA by all three major rating agencies (Fitch, Moody's and Standard and Poors); and
- iii. the Council's investments with the bank are limited to amounts and maturities within the terms of the stipulated guarantee.

- Banks 3 – Part nationalised UK banks – Lloyds Banking Group and Royal Bank of Scotland Group. These banks can be included if they continue to be part nationalised or they meet the above criteria.
- Banks 4 – The Council's own banker for transactional purposes if the bank falls below the above criteria, although in this case balances will be minimised in both monetary size and time.
- Bank subsidiary and treasury operations - The Council will use these where the parent bank has the necessary ratings outlined above.
- Building societies: The Council will use all societies which meet the ratings for banks outlined above.
- Money market funds (including enhanced money market funds) – AAA
- UK Government (including gilts and the DMADF)
- Local authorities, parish councils etc
- Supranational institutions

A limit of £5m will be applied to the use of non-specified investments (investments with a maturity of over 364 days but not more than 370 days).

**Country and sector considerations** - Due care will be taken to consider the country, group and sector exposure of the Council's investments. In part, the country selection will be chosen by the credit rating of the sovereign state in Banks 1 above. In addition:

- no more than £4m will be placed with any non-UK country at any time;
- limits in place above will apply to a group of companies;
- sector limits will be monitored regularly for appropriateness.

**Use of additional information other than credit ratings.** Additional requirements under the Code require the Council to supplement credit rating information. Whilst the above criteria relies primarily on the application of credit ratings to provide a pool of appropriate counterparties for officers to use, additional operational market information will be applied before making

**Deleted:** <#>Viability (Fitch) / Financial Strength (Moody's) – ¶¶  
<#>bb- (Fitch) / C- (Moody's)¶¶  
Support – 3 (Fitch only)



any specific investment decision from the agreed pool of counterparties. This additional market information (for example Credit Default Swaps, negative rating watches/outlooks) will be applied to compare the relative security of differing investment counterparties.

**Time and monetary limits applying to investments.** The time and monetary limits for institutions on the Council's counterparty list are as follows (these will cover both specified and non-specified investments):

	Fitch Long term Rating (or equivalent)		Money Limit	Time Limit	Deleted: Fitch Viability Rating / Moody's Financial Strength Rating
Higher quality	AA-		£6m	370	Deleted: bb+ / C
Medium quality (1)	A		£5m	370	Deleted: bb+ / C
					Deleted: Medium quality (2)
Part nationalised	N/A		£7m	370	Deleted: A
Debt Management Account Deposit Facility	AAA		unlimited	6 months	Deleted: bb- / C- Deleted: £4m
Guaranteed Organisations	N/A		£4m	370	Deleted: 370 days
Money market Funds (including enhanced money market funds)	AAA		£5m	370	Deleted: N/A Deleted: N/A
Local authorities	N/A		£4m	370	Deleted: N/A Deleted: N/A

The proposed criteria for specified and non-specified investments are shown in section 5 for approval.

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## THANET DISTRICT COUNCIL DECLARATION OF INTEREST FORM

### Do I have a Disclosable Pecuniary Interest and if so what action should I take?

Your Disclosable Pecuniary Interests (DPI) are those interests that are, or should be, listed on your Register of Interest Form.

If you are at a meeting and the subject relating to one of your DPIs is to be discussed, in so far as you are aware of the DPI, you **must** declare the existence **and** explain the nature of the DPI during the declarations of interest agenda item, at the commencement of the item under discussion, or when the interest has become apparent

Once you have declared that you have a DPI (unless you have been granted a dispensation by the Standards Committee or the Monitoring Officer, for which you will have applied to the Monitoring Officer prior to the meeting) you **must:-**

1. Not speak or vote on the matter;
2. Withdraw from the meeting room during the consideration of the matter;
3. Not seek to improperly influence the decision on the matter.

### Do I have a significant interest and if so what action should I take?

A significant interest is an interest (other than a DPI or an interest in an Authority Function) which:

1. Affects the financial position of yourself and/or an associated person; or Relates to the determination of your application for any approval, consent, licence, permission or registration made by, or on your behalf of, you and/or an associated person;
2. And which, in either case, a member of the public with knowledge of the relevant facts would reasonably regard as being so significant that it is likely to prejudice your judgment of the public interest.

An associated person is defined as:

- A family member or any other person with whom you have a close association, including your spouse, civil partner, or somebody with whom you are living as a husband or wife, or as if you are civil partners; or
- Any person or body who employs or has appointed such persons, any firm in which they are a partner, or any company of which they are directors; or
- Any person or body in whom such persons have a beneficial interest in a class of securities exceeding the nominal value of £25,000;
- Any body of which you are in a position of general control or management and to which you are appointed or nominated by the Authority; or
- any body in respect of which you are in a position of general control or management and which:
  - exercises functions of a public nature; or
  - is directed to charitable purposes; or
  - has as its principal purpose or one of its principal purposes the influence of public opinion or policy (including any political party or trade union)

An Authority Function is defined as: -

- Housing - where you are a tenant of the Council provided that those functions do not relate particularly to your tenancy or lease; or
- Any allowance, payment or indemnity given to members of the Council;
- Any ceremonial honour given to members of the Council
- Setting the Council Tax or a precept under the Local Government Finance Act 1992

If you are at a meeting and you think that you have a significant interest then you **must** declare the existence **and** nature of the significant interest at the commencement of the

matter, or when the interest has become apparent, or the declarations of interest agenda item.

Once you have declared that you have a significant interest (unless you have been granted a dispensation by the Standards Committee or the Monitoring Officer, for which you will have applied to the Monitoring Officer prior to the meeting) you **must**:-

1. Not speak or vote (unless the public have speaking rights, or you are present to make representations, answer questions or to give evidence relating to the business being discussed in which case you can speak only)
2. Withdraw from the meeting during consideration of the matter or immediately after speaking.
3. Not seek to improperly influence the decision.

### **Gifts, Benefits and Hospitality**

Councillors must declare at meetings any gift, benefit or hospitality with an estimated value (or cumulative value if a series of gifts etc.) of £100 or more. You **must**, at the commencement of the meeting or when the interest becomes apparent, disclose the existence and nature of the gift, benefit or hospitality, the identity of the donor and how the business under consideration relates to that person or body. However you can stay in the meeting unless it constitutes a significant interest, in which case it should be declared as outlined above.

### **What if I am unsure?**

If you are in any doubt, Members are strongly advised to seek advice from the Monitoring Officer or the Democratic Services and Scrutiny Manager well in advance of the meeting.

## **DECLARATION OF DISCLOSABLE PECUNIARY INTERESTS, SIGNIFICANT INTERESTS AND GIFTS, BENEFITS AND HOSPITALITY**

**MEETING**.....

**DATE**..... **AGENDA ITEM** .....

**DISCRETIONARY PECUNIARY INTEREST**

**SIGNIFICANT INTEREST**

**GIFTS, BENEFITS AND HOSPITALITY**

**THE NATURE OF THE INTEREST, GIFT, BENEFITS OR HOSPITALITY:**

.....  
.....  
.....

**NAME (PRINT):** .....

**SIGNATURE:** .....

Please detach and hand this form to the Democratic Services Officer when you are asked to declare any interests.