TREASURY MANAGEMENT QUARTERLY UPDATE

To:	**Governance and Audit Committee – 20 March 2012**
Main Portfolio Area:	**Finance and Corporate Services**
By:	**Finance Manager (Capital, HRA and External Funding)**
Classification:	**Unrestricted**

Summary: **To update Governance and Audit Committee on Treasury activity since the last report.**

<u>For Information</u>

1.0 Introduction and Background

1.1 This report is to update Members on what Treasury activity has taken place since the last Governance and Audit Committee meeting on 13th December 2011.

2.0 Treasury Management

2.1 The base rate has stayed at 0.5% and the new forecasts just released from our Treasury consultants show that this is expected to remain the case for the remainder of the year.

2.2 A £1m investment has been placed in new 10 day notice account which has been opened with Svenska Handlesbanken offering a rate of 0.60%. This will extend our counterparty options and offers comparable rates with other accounts the authority holds.

2.3 Santander UK plc has recently been downgraded and whilst still on the authority's counterparty list as it continues to be on a negative ratings watch funds have been withdrawn.

2.4 Time deposits with Lloyds TSB (interest rate of 1.35%) and NatWest (interest rate of 1.15%) have been recalled to aid with the authority's cash flow during the months of February and March due to Council Tax receipts not being due.

2.5 In the new financial year a review of Time deposit products will be undertaken in line with the authority's cash flow needs to try to take advantage of the longer term investments that offer the most attractive rates with out jeopardising the Council's liquidity or security requirements.

2.6 A £3m Public Works and Loan Board loan became due for re-payment on the 31st December 2011 and has subsequently been repaid.

3.0 HRA Self-Financing Loan Portfolio

3.1 HRA Self-financing becomes compulsory through legislative changes in the Localism Bill from 1 April 2012. The proposal is based on moving towards a 'self-financing' HRA system in which negative or positive subsidy would be exchanged for a single one-off adjustment of housing debt, following which rental surpluses would be retained 100% by local authorities. The settlement for Thanet District Council has resulted in a one off re-payment of debt of £925k. This will be paid by top slicing the authority's existing loan portfolio held by the PWLB (Public Works Loan Board).

3.2 Currently the authority's loan portfolio is held in one single pool and the costs of borrowing are apportioned across the HRA and General Fund using a complex calculation as set out in the subsidy determination. As part of the self-financing review this arrangement has also been looked at to see if it should be amended.

3.3 The following options have been proposed and some guidance has been given to the advantages and disadvantages of the options:-

One Pool Approach

Advantage	Disadvantage	Thanet Perspective
A single pool would be able to manage the debt portfolio to take advantage of the preferential rates offered for PWLB self-financing loans by reducing the overall average rate of interest chargeable to both the GF and HRA.	The full benefit of any preferential rates for self-financing loans would not be fully passed on the HRA.	As Thanet will not be taking on any debt there will be no large loans at a preferential rate to take advantage of this and effect a saving to the general fund.
Refinancing risks shared across the General Fund and HRA, reducing the risk to both.	Lack of certainty for HRA planning purposes.	In the past the HRA has been affected by re-newed loans reduced borrowing rates to benefit the General Fund.
Simple to manage under existing arrangements	Loans not physically split between General Fund and HRA in line with the sentiment of self-financing	There would be less officer administration required maintaining one pool as opposed to two or three.
Cost of new borrowing (including self-financing) would be shared between the General Fund and HRA.	HRA Strategic options restricted as the impact on the General Fund would have to be considered.	Any new borrowing that the General Fund undertook would impact on the HRA and vice versa.
Increased flexibility to repay debt as and when business/spending plans allow	Decisions taken on the repayment of debt will affect both the General Fund and the HRA.	Consideration will have to be given to the affordability for both pools for the repayment of any debt.

Two Pool Approach

Advantage	Disadvantage	Thanet Perspective
HRA could immediately benefit from the preferential rates offered for self-financing borrowing	Any re-financing risk would be at a higher rate and fall to the HRA.	Thanet is not taking on any debt and so will not have any preferential rate borrowing.
HRA debt would be managed independently from the General Fund and vice versa	Would require a clear understanding of asset management requirements to avoid the risk of carrying unnecessary debt	Both the General Fund and HRA are undertaking a review of their asset management requirements.
HRA would inherit fixed costs in relation to debt costs to assist with the business plan modelling and increase certainty	Options to repay debt or react to changes in market conditions would be restricted.	The HRA has sufficient balances that could be modelled to repay debt as and when it is due.
Separate Treasury Management Strategy for General Fund and HRA to meet individual requirements.	The HRA may want to develop its own approach to Treasury Management.	The current Treasury Strategy is adequate to meet the requirements of both funds. Although this is something that will need to be reviewed on a yearly basis.
General Fund and HRA debt costs and borrowing levels are not influenced by each others long term strategy.	Each fund will take on a greater degree of risk as they will not be able to spread the risk between the two funds.	Currently any decisions taken to borrow or repay debt affect both funds. In the event that they have two pools they will each have an independence to make the right decision for each fund.
Loans are split between HRA and General Fund based on the capital financing requirement for each fund.	Greater administration required as two loan pools will need to be maintained.	Thanet currently only has one Treasury Officer undertaking this work. A review of current working practice would need to be undertaken to create resilience.

3.4 There is one final option which is the Three Pool approach which requires the existing debt pool to become one residual pool, which will reduce in value as debt is repaid at maturity or earlier. Borrowing for new capital expenditure, including the settlement payment, additional debt to cover under-borrowing and replacement debt would then be allocated to the two new separate pools one for Housing and one for General Fund.

3.5 CIPFA guidance issued favours the two pool approach although it is left to the authority to decide the best approach that does not result in a disproportionate charge to either the Housing Revenue Account or the General Fund. It is therefore recommended that the authority rules out the one pool approach due to the impact of future borrowing on both funds, although there would be an increased exposure to interest rate risk when re-financing and considers only the two pool or three pool approach. Whilst there will be increased administration required, the two pool approach will require slightly less administration compared to the three pool approach and so it proposed that the authority undertakes a two pool approach for debt from 1 April 2012.

3.6 Local authorities are normally required each year to set aside some of their revenues as provision for debt. The provision is in respect of capital expenditure financed by borrowing or credit arrangements; this is known as the minimum revenue provision. Amendments have been made to the Local Authorities Capital Finance and Accounting Regulations 2003 and 2008 to ensure that those authorities that have to take on a higher level of debt through self-financing and therefore increase their capital financing requirement (CFR) do not incur an increased revenue charge by making the usual minimum revenue provision (MRP). The Secretary of State considers that, given the special circumstances of the exercise, such consequence should not be imposed upon authorities. Therefore, formal recommendation was made that for the purposes of determining the minimum revenue provision this increase in the capital financing requirement may be ignored and avoid any impact on the revenue budget. As Thanet is not taking on any new debt within the settlement the minimum provision set aside remains largely unchanged as a result of self-financing.

3.7 A more detailed report on the HRA Self-Financing settlement is due to go to Cabinet for 29 March 2012.

4.0 Corporate Implications

4.1 Financial and VAT

4.1.1 The Financial implications are reflected within the body of this report and supporting annexes. Until the PWLB loans settlement takes place it is difficult to quantify the savings that will be achieved as the payment is to be top sliced across the whole PWLB loan portfolio. However, initial work undertaken supports that moving to a two pool loan portfolio would not be a financial detriment to either the General Fund or Housing Revenue Account in line with CIPFA guidance.

4.1.2 There are no VAT implications with this report.

4.2 Legal

4.2.1 There are no legal implications arising directly from this report.

4.3 Corporate

4.3.1 Failure to undertake this process will impact on the authority’s compliance with the Treasury Management Code of Practice.

4.4 Equity and Equalities

4.4.1 There are no equalities issues arising from this report.

5.0 Recommendation(s)

6.1 That members note the content of this report.

6.0 Decision Making Process

6.1 Under the treasury Management Code of Practice it is required that the Governance and Audit Committee note this report.

Contact Officer:	Nicola Walker (Finance Manager-HRA, Capital and External Funding)
Reporting to:	Sarah Martin – Financial Services Manager

Background Papers

Title	**Details of where to access copy**
Council Housing: a real future – Impact Assessment	*www.communities.gov.uk*
Proposals for the Reform of HRA Subsidy System	*Cabinet 17 June 2010*
Implementing Self-financing for Council Housing	*www.communities.gov.uk*
Self-financing: Planning the transition	*www.communties.gov.uk*

Corporate Consultation Undertaken

Finance	Sarah Martin
Legal	Gary Cordes
Communications	Justine Wingate