Appendix 1 - Treasury Strategy, Minimum Revenue Position Policy

PETERBOROUGH CITY COUNCIL

Treasury Management Strategy 2016/17 to 2025/26

Including:

Revised Minimum Revenue Provision Policy 2015/16

Minimum Revenue Provision Policy 2016/17

1. Introduction

1.1 Background

1.1.1 The Council is required to operate a balanced budget, which means that cash raised through the year will meet cash expenditure. The role of treasury management is to ensure cash flow is adequately planned so that cash is available when it is needed. Surplus monies are invested in low risk counterparties commensurate with the Council's low risk appetite ensuring that security and liquidity are achieved before considering investment return.

1.1.2 Another role of treasury management is to fund the Council's capital programme. The programme provides a guide to the borrowing needs of the Council and the planning of a longer term cash flow to ensure capital obligations are met. The management of long term cash may involve arranging short or long term loans or using longer term cash flow surpluses.

1.1.3 CIPFA defines treasury management 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."

1.2 Reporting requirements

1.2.1 The Council is required to receive and approve, as a minimum, three reports each year. These reports are to be scrutinised by the Audit Committee before being recommended to Council.

1.2.2 The Treasury Management Strategy report will cover:

- the capital programme (including prudential indicators)
- a Minimum Revenue Provision (MRP) Policy
- the Treasury Management Strategy including treasury indicators; and
- an Investment Strategy

1.2.3 A mid-year Treasury Management Report will update members of the Audit Committee with the progress of the capital programme and amending prudential indicators as necessary.

1.2.4 Any revisions to the Treasury Strategy will need to be approved by Full Council.

1.2.5 An Annual Treasury Report will provide details of actual prudential and treasury indicators and actual treasury operations compared to the estimates within the strategy presented alongside the Statement of Accounts.

1.3 Treasury Management Strategy for 2016/17

1.3.1 The strategy for 2016/17 will cover

- Policy on use of external advisors
- Capital programme and the Prudential Indicators
- MRP strategy and policy
- Current treasury position
- Treasury indicators
- Interest rates
- Borrowing strategy
- Policy on borrowing in advance of need
- Debt rescheduling
- Investment strategy
- Creditworthiness policy
- Treasury Management Scheme of Delegation

1.3.2 These elements cover the requirements of the Local Government Act 2003, the CIPFA Prudential Code, the Communities and Local Government (CLG) MRP Guidance, the CIPFA Treasury Management Code and the CLG Investment Guidance.

1.4 Treasury Management Advisors

1.4.1 The Council uses Capita Asset Services, as its external treasury management advisors who have a contract until December 2017.

1.4.2 The Council recognises that responsibility for treasury management decisions remain with the organisation at all times and will ensure that undue reliance is not placed upon external advisors.

1.4.3 The Council also recognises that there is value in employing external providers of treasury management services in order to acquire access to specialist skills and resources. The Council will ensure that the terms of their appointment and the methods by which their value will be assessed are properly agreed and documented and subjected to regular review.

2. Capital Prudential Indicators 2016/17 to 2025/26

2.1.1 The Council's capital programme is the key driver of the treasury management activity. The output of the capital programme is reflected in the prudential indicators which are designed to assist member's overview and confirm the capital programme.

2.1.2 **Indicator 1** – Capital Expenditure – this Prudential Indicator is a summary of the Council's estimated capital expenditure for the forthcoming financial year and the following nine financial years.

(1a) Capital Expenditure	2014/15 Actuals £m	2015/16 Est. £m	2016/17 Est. £m	2017/18 Est. £m	2018/19 Est. £m	2019/20 Est. £m	2020/21 Est. £m	2021/22 Est. £m	2022/23 Est. £m	2023/24 Est. £m	2024/25 Est. £m	2025/26 Est. £m
Governance	*0.1*	0.4	-	-	-	-	-	-	-	-	-	-
People & Communities	*56.4*	32.2	37.1	16.4	26.0	16.6	7.8	3.5	3.5	3.5	3.5	3.5
Resources	*21.8*	39.8	25.4	4.2	4.9	4.9	4.0	4.7	4.8	4.8	4.8	4.8
Growth & Regeneration	*26.2*	20.8	37.6	33.5	19.2	8.7	6.4	6.4	6.4	6.4	6.4	7.3
Invest to Save	*4.3*	61.9	56.5	60.0	35.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Total	***108.8***	**155.1**	**156.6**	**114.1**	**85.1**	**30.2**	**18.2**	**14.6**	**14.7**	**14.7**	**14.7**	**15.6**
Financed by:												
Capital receipts	*2.9*	-	1.0	-	1.0	-	-	-	-	-	-	-
Capital grants & contributions	*35.6*	25.4	33.7	20.0	10.5	8.5	7.5	5.4	5.6	5.6	5.6	5.6
Net financing requirement	***70.3***	**129.7**	**121.9**	**94.1**	**73.6**	**21.7**	**10.7**	**9.2**	**9.1**	**9.1**	**9.1**	**10.0**
Total	***108.8***	**155.1**	**156.6**	**114.1**	**85.1**	**30.2**	**18.2**	**14.6**	**14.7**	**14.7**	**14.7**	**15.6**

2.2 The previous table summarises the capital expenditure which is shown in more detail in the Capital Strategy Annex One including how it will be funded either from grants, contributions, or capital receipts with the remaining 'net financing need for the year' to be sourced via borrowing. The capital receipts shown in the tables for future years relate to the return of the LAMS capital loan.

2.3 The Invest to Save scheme, Renewable Energy projects and the Energy from Waste plant are included in the tables that detail total capital expenditure and the funding resources to be used. However, these schemes will either generate income, generate savings, or avoid additional costs e.g. landfill tax. Therefore the borrowing costs associated with these projects will have a minimal impact on the Council's MTFS position.

2.4 **Indicator 2** – Capital Financing Requirement (CFR) – the CFR is the total historic capital expenditure which has not yet been paid for from either revenue or capital resources. It is a measure of the Council's underlying borrowing requirement. Any capital expenditure which has not immediately been paid for will increase the CFR.

2.5 The CFR includes any other long term liabilities (e.g. PFI schemes, finance leases) included on the Council's balance sheet following the IFRS conversion in 2010/11. Whilst this increases the CFR, and therefore the Council's borrowing requirement, these types of schemes include a borrowing facility and so the Council is not required to separately borrow for these schemes.

2.6 The following table shows the CFR estimates for the next ten financial years:

(2) Capital Financing Requirement	**2014/15 Actuals £m**	**2015/16 Est. £m**	**2016/17 Est. £m**	**2017/18 Est. £m**	**2018/19 Est. £m**	**2019/20 Est. £m**	**2020/21 Est. £m**	**2021/22 Est. £m**	**2022/23 Est. £m**	**2023/2 4Est. £m**	**2024/25 Est. £m**	**2025/26 Est. £m**
CFR B/fwd	*365.6*	422.5	546.0	658.3	663.8	726.1	735.9	734.4	730.7	727.2	723.1	718.4
Borrowing	*53.3*	61.6	52.3	(54.7)	27.3	9.8	(1.5)	(3.7)	(3.5)	(4.1)	(4.7)	(4.4)
Invest to Save*	*3.6*	61.9	60.0	60.0	35.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
CFR C/fwd	*422.5*	546.0	658.3	663.6	726.1	735.9	734.4	730.7	727.2	723.1	718.4	714.0
Movement in CFR	***56.7***	**123.5**	**112.3**	**5.4**	**62.3**	**9.8**	**(1.5)**	**(3.7)**	**(3.5)**	**(4.1)**	**(4.7)**	**(4.4)**
Net financing requirement	*70.3*	129.7	121.9	94.1	73.6	21.7	10.7	9.3	9.2	9.2	9.2	10.1
Less MRP & other financing	*(13.6)*	(6.2)	(9.6)	(88.7)#	(11.3)	(11.9)	(12.2)	(13.0)	(12.7)	(13.3)	(13.9)	(14.5)
Movement in CFR	***56.7***	**123.5**	**112.3**	**5.4**	**62.3**	**9.8**	**(1.5)**	**(3.7)**	**(3.5)**	**(4.1)**	**(4.7)**	**(4.4)**

** The cost of borrowing associated with this scheme will be offset by the income generated in accordance with the approved business case (see comment in 2.3)*
 # This includes the ECS Peterborough 1 LLP loan repayment of £77m which is the level that has been approved but not yet utilised

2.7 **Indicator 3** – Actual and estimates of the ratio of financing costs to net revenue budget. This indicator identifies the proportion of the revenue budget which is taken up in financing capital expenditure i.e. the net interest cost and the provision to repay debt.

3) Ratio of financing costs to net revenue budget	**2014/15 Actuals £m**	**2015/16 Est. £m**	**2016/17 Est. £m**	**2017/18 Est. £m**	**2018/19 Est. £m**	**2019/20 Est. £m**	**2020/21 Est. £m**	**2021/22 Est. £m**	**2022/23 Est. £m**	**2023/2 4Est. £m**	**2024/25 Est. £m**	**2025/26 Est. £m**
Total ratio	*5.9%*	4.3%	6.1%	7.4%	8.1%	8.6%	8.7%	8.5%	8.4%	8.4%	8.3%	8.2%

2.8 **Indicator 4** – Actual and estimates of the incremental impact of capital investment decisions on council tax. The calculation of this indicator is based upon the estimated amount of the capital programme that is to be financed from borrowing.

2.9 The calculation is based on the interest assumptions for borrowing and MRP charges that have been included in the previous and this MTFS for the capital financing budget.

2.10 This indicator is showing the incremental impact of capital investment decisions along with the amendments to the MRP policy as contained in the following section, see point 3.

2.11 This indicator shows the incremental impact on the 'adjusted' council tax base.

(4) Incremental impact of capital investment decisions on Council Tax	**2014/15 Actuals £**	**2015/16 Est. £**	**2016/17 Est. £**	**2017/18 Est. £**	**2018/19 Est. £**	**2019/20 Est. £**	**2020/21 Est. £**	**2021/22 Est. £**	**2022/23 Est. £**	**2023/24 Est. £**	**2024/25 Est. £**	**2025/26 Est. £**
Incremental change in capital financing budget between MTFS's on Band D Council Tax (£)	*(82.17)*	*(307.41)*	(197.70)	(115.10)	(73.51)	(31.59)	(24.63)	7.12	(5.61)	(8.11)	(10.36)	(15.83)

3. Minimum Revenue Provision (MRP) Policy

3.1. Capital expenditure is generally expenditure on assets which have a life expectancy of more than one year e.g. buildings, vehicles, equipment, etc. Such expenditure is spread over several years in order to try to match the years over which such assets benefit the local community through their useful life. The manner of spreading these costs is through an annual Minimum Revenue Provision (MRP).

3.2. CLG Regulations require full Council to approve a MRP statement in advance of each year. A variety of options are provided to Councils to calculate this revenue charge and the Council must satisfy itself that the provision is prudent.

3.3. A comprehensive review of the Council's method for calculating its MRP has been undertaken in order to ensure that the amount of revenue put aside to repayment debt represents a fair charge compared to the life of the asset that is being financed via borrowing. Further details of the amendments to the Council's MRP policy are contained in the table in Appendix 3.

3.4. The Council is recommended to approve the amendments to the 2015/16 MRP policy and to approve MRP policy for 2016/17 as summarised in the following table. These policies ensure that the Council satisfies the requirement to set aside a prudent level of MRP.

3.5. Councils are allowed by statute to use capital receipts for the repayment of any borrowing previously incurred. The application of capital receipts to repay debt would reduce the level of MRP chargeable to revenue, but statutory guidance does not address how such a reduction should be calculated. The Council proposes that in years when it uses capital receipts to redeem borrowing, the value of the MRP which would otherwise have been set aside for that year will be reduced by the amounts which have instead been repaid from capital receipts. This will still result in a prudent level of MRP, as there will be no reduction in the overall level of funding set aside to redeem debt.

3.6. The Council intends to make secured loans to third parties. These loans are only made after the Council's formal decision making process has been followed, which includes formal approval by the Service Director Financial Services. As part of the formal decision to grant the loan, the security for the loan will be assessed as to its adequacy in the event of the third party defaulting on repayment. The Council have approved the secured loans to two third parties which are Axiom Housing Association (Council - 8 October 2014), ECS Peterborough 1 LLP (Council - 17 December 2014) and the Housing Joint Venture subject to Cabinet approval. The Council has held some preliminary discussions with Peterborough Regional College regarding the possibility of the Council lending to them to invest in new facilities. These discussions are at a very early stage, but it is recommended that PRC are added to the list of organisations the Council can make secured loans to. This does not commit the Council making such a loan, it simply means that the Council can consider this during the year. This could only proceed following an appropriate executive decision'

3.7. The Council participates in the Local Authority Mortgage Scheme (LAMS). During 2011/12 the Council deposited £1m with Lloyds and a further £1m during 2013/14. Such deposits are treated as capital expenditure, as a loan to a third party. The CFR increased by the total of these indemnities. Operation of the Scheme sees these deposits returned in full at maturity, a period of five years, with interest paid annually. Once the deposit matures, and funds are returned to the Council, the funds are classed as a capital receipt (as it is a loan) and the CFR will reduce accordingly. As this is a temporary five year arrangement and the funds are anticipated to be returned in full, there is no MRP application. The Council has agreed to place a proportion of the interest received on the deposit into an earmarked reserve to mitigate the impact if the indemnity is used over that period of the Scheme.

3.8. Repayments for PFI scheme and finance leases are applied as MRP, and the associated amounts are included in these Prudential Indicators.

Capital Expenditure Incurred	MRP Policy 2015/16	Revised MRP Policy 2015/16 & MRP Policy for 2016/17
Pre 2007/08 debt (ie debt up to 31.03.2007)	Charged 4% reducing balance (Option 1)	Use the annuity method of calculation over an average weighted asset life
Supported Borrowing post 2007/08		
Unsupported borrowing 2007/08 & 2008/09	Charged in relation to asset life on equal instalment method	Use the annuity method of calculation over the remaining asset life
Unsupported borrowing Post 2008/09	Charged in relation to asset life on annuity method	Charged in relation to asset life on annuity method
Private Finance Initiative (PFI) - Finance Lease	Charged derived from using the PFI model	Use the annuity method of calculation over the remaining asset life
Other Finance Leases	Charged in relation to asset life on annuity method	Charged in relation to asset life on annuity method
Expenditure funded by unsupported borrowing reflected within the debt liability after the 31 March 2010	Asset Life Method, annuity method – MRP will be based on the prevailing PWLB interest rate for a loan with a term equivalent to the estimated life of the project.	Asset Life Method, annuity method – MRP will be based on the prevailing PWLB interest rate for a loan with a term equivalent to the estimated life of the project. If capital receipts have been used to repay borrowing for the year then the value of MRP which would have otherwise been set aside to repay borrowing will be reduced by the amounts which have instead been repaid from capital receipts. The level of capital receipts to be applied to redeem borrowing will be determined annually by the Corporate Director Resources, taking into account forecasts for future expenditure and the generation of further receipts.
Expenditure investing in third parties via a loan which is fully secured and where repayment is in bullet form.	The Council considers the repayment of the loan negates the need for an amount of MRP to be charged each year as reliance can be placed on the capital receipt that will be generated when the loan is repaid or, in the event of a default, the realisation of the security	The Council considers the repayment of the loan negates the need for an amount of MRP to be charged each year as reliance can be placed on the capital receipt that will be generated when the loan is repaid or, in the event of a default, the realisation of the security

For more detailed guidance on MRP see the CLG website https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/11297/2089512.pdf

4. Treasury Management Strategy

4.1. Treasury Management Policy

4.1.1. The treasury management function ensures that the Council's cash is managed in accordance with the relevant professional codes, so that sufficient cash is available to meet the Council's service requirements. This will involve both the management of cash flow and, where the capital programme requires, the organisation of appropriate borrowing facilities. This strategy covers the relevant treasury / prudential indicators, the current and projected debt positions, and the Annual Investment Strategy.

4.1.2. The Council's primary treasury management objectives are:

a) to invest available cash balances with a number of high quality investment counterparties (see 4.8.12) over a

spread of maturity dates in accordance with the Council's lending list;

b) to reduce the revenue cost of the Council's debt in the medium term by obtaining financing at the cheapest rate possible; and

c) to seek to reschedule debt at the optimum time.

4.2 Current Treasury Position

4.2.1 **Indicator 5** - The Council's treasury position at 31 March 2015, with estimates for future years, are summarised below. The table below shows the actual external borrowing (Gross Debt) against the CFR.

(5) Gross debt & capital financing requirement	2014/15 Actuals £m	2015/16 Est. £m	2016/17 Est. £m	2017/18 Est. £m	2018/19 Est. £m	2019/20 Est. £m	2020/21 Est. £m	2021/22 Est. £m	2022/23 Est. £m	2023/2 4Est. £m	2024/25 Est. £m	2025/26 Est. £m
External Borrowing												
Market Borrowing	*306.0*	311.8	431.5	545.5	515.5	579.1	590.2	595.1	599.9	604.5	609.1	613.8
Repayment of borrowing	-	(17.0)	(22.0)	(56.0)	(9.0)	(8.0)	(15.0)	(8.0)	(7.1)	-	(8.0)	-
Expected change in borrowing	-	142.5	136.0	26.0	72.6	19.1	19.9	12.8	11.7	4.7	12.7	4.6
Other long-term liabilities	*40.4*	39.5	38.6	37.8	37.0	36.2	35.4	34.9	34.3	33.7	33.0	32.3
Gross Debt at 31 March	***346.4***	**470.9**	**584.1**	**553.3**	**616.1**	**626.4**	**630.5**	**634.8**	**638.8**	**642.8**	**646.9**	**650.7**
CFR	422.5	546.0	658.4	663.8	726.1	735.9	734.4	730.7	727.2	723.1	718.4	714.0
% of Gross Debt to CFR	***82.0%***	**86.2%**	**88.7%**	**83.4%**	**84.9%**	**85.1%**	**85.9%**	**86.9%**	**87.8%**	**88.9%**	**90.0%**	**91.1%**

4.2.2 Within the prudential indicators there are a number of key indicators to ensure that the Council operates its activities within defined limits. One of these is that the Council needs to ensure that its total borrowing does not, except in the short term, exceed the total of the CFR in the year plus the estimates of any additional CFR for 2016/17 and the following two financial years. This allows some flexibility for limited early borrowing for future years, but ensures that borrowing is not undertaken for revenue purposes.

4.2.3 The Corporate Director Resources reports that the Council complied with this prudential indicator in the current year and

4.2.4 does not envisage difficulties for the future. This view takes into account current commitments, existing plans and the proposals in this medium term financial strategy (MTFS).

4.2.5 **Indicator 6** - The Operational Boundary - this is the limit beyond which external borrowing is not normally expected to exceed. If the operational boundary was exceeded this would be reported immediately to the members of the Audit Committee with a full report taken to the next committee meeting. In the current year it has not been exceeded.

(6) Operational Boundary	**2014/15 Actuals £m**	**2015/16 Est. £m**	**2016/17 Est. £m**	**2017/18 Est. £m**	**2018/19 Est. £m**	**2019/20 Est. £m**	**2020/21 Est. £m**	**2021/22 Est. £m**	**2022/23 Est. £m**	**2023/2 4Est. £m**	**2024/25 Est. £m**	**2025/26 Est. £m**
Borrowing	*306.0*	588.6	690.9	686.3	693.3	646.3	640.5	639.8	638.8	642.8	646.9	646.9
Other long term liabilities	*40.4*	39.5	38.6	37.8	37.0	36.2	35.4	34.9	34.3	33.7	33.0	32.3
Total	***346.4***	**628.1**	**729.5**	**754.1**	**730.3**	**682.5**	**676.0**	**674.7**	**673.1**	**676.5**	**679.9**	**679.2**

4.2.6 **Indicator 7** - The Authorised Limit for external borrowing - this represents a limit beyond which external borrowing is prohibited, and this limit needs to be set or revised by full Council.

4.2.7 This is a statutory limit determined under section 3 (1) of the Local Government Act 2003. The Government retains an option to control either the total of all Council's plans, or those of a specific Council, although this power has not yet been exercised.

4.2.8 The Council is asked to approved the following Authorised limit:

(7) Authorised Limit	**2014/15 Actuals £m**	**2015/16 Est. £m**	**2016/17 Est. £m**	**2017/18 Est. £m**	**2018/19 Est. £m**	**2019/20 Est. £m**	**2020/21 Est. £m**	**2021/22 Est. £m**	**2022/23 Est. £m**	**2023/2 4Est. £m**	**2024/25 Est. £m**	**2025/26 Est. £m**
Borrowing	*306.0*	665.6	796.6	796.1	745.2	686.2	677.5	676.6	674.3	677.1	680.8	682.2
Other long term liabilities	*40.4*	39.5	38.6	37.8	37.0	36.2	35.4	34.9	34.3	33.7	33.0	32.3
Total	***346.4***	**705.1**	**835.2**	**833.9**	**782.2**	**722.4**	**712.9**	**711.5**	**708.6**	**710.8**	**713.8**	**714.5**

Prospects for interest rates

4.2.9 The Council utilises the treasury services of Capita Asset Services and part of their service is to assist the Council to formulate a view on interest rates to assist with borrowing and investment decisions. The Capita Asset Services forecast for bank base rate (as at January 2016) and PWLB new borrowing (as at November 2015) is as follows (note that the PWLB Borrowing Rate includes the Certainty Rate adjustment):

Interest Rate (All rates shown as %)	**Now**	**Mar 16**	**Jun 16**	**Sep 16**	**Dec 16**	**Mar 17**	**Jun 17**	**Sep 17**	**Dec 17**	**Mar 18**	**Jun 18**	**Sep 18**	**Dec 18**	**Mar 19**
Bank Rate View	0.50	0.50	0.50	0.50	0.75	0.75	1.00	1.00	1.25	1.25	1.50	1.50	1.75	1.75
5yr PWLB Rate	2.30	2.40	2.60	2.70	2.80	2.80	2.90	3.00	3.20	3.30	3.40	3.50	3.50	3.60
10yr PWLB Rate	2.90	3.00	3.10	3.20	3.30	3.40	3.50	3.60	3.70	3.80	3.90	4.00	4.10	4.10
25yr PWLB Rate	3.60	3.70	3.80	3.90	4.00	4.10	4.10	4.20	4.30	4.30	4.40	4.40	4.40	4.50
50yr PWLB Rate	3.50	3.60	3.70	3.80	3.90	4.40	4.00	4.00	4.10	4.20	4.30	4.30	4.30	4.40
Budget Assumption	3.43		3.85				4.08				4.33			

4.2.10 The Council successfully applied to be one of the principal local authorities that would qualify for the Certainty Rate, during the period 1 November 2015 to 31 October 2016. This results in the Council being able to benefit from reduced interest rates on PWLB loans by 20 basis points (0.20%). The council is assuming that there will be a similar scheme in place when this scheme expires. The Council will submit a new application to ensure it qualifies.

4.2.11 The MTFS assumes borrowing is taken at the 50 year period with an average taken across the quarters for that year but then adjusted with a range of borrowing periods and associated interest rates. The Chief Finance Officer believes this prudent as it mitigates some of the risk of PWLB rate rise.

4.2.12 Capita Asset Services interest rate forecasts, detailed above, are based on their views of the future economic climate, and below are some extracts taken from their economic forecasts:

- Economic forecasting remains difficult with so many external influences weighting on the UK. Capita Asset Services Bank Rate forecasts, (and also MPC decisions), will be liable to further amendment depending on how the economic data and developments in financial markets transpire over the next year. Forecast for average earnings beyond the three year horizon will be heavily dependent on economic and political developments. Major volatility in bond yields is likely to endure as investor fears and confidence ebb and flow between favouring more risky assets or the safe haven of bonds.
- The November Inflation Report flagged up particular concerns for the potential impact of these factors on the UK.

The Inflation Report was also notably subdued in respect of the forecasts for inflation; this was expected to barely get back up to the 2% target within the 2-3 year time horizon. The increase in the forecast for inflation at the three year horizon was the biggest in a decade and at the two year horizon was the biggest since February 2013.

- However, the first round of falls in oil, gas and food prices over late 2014 and also in the first half 2015, will fall out of the 12 month calculation of CPI during late 2015 / early 2016 but a second, more recent round of falls in fuel and commodity prices will delay a significant tick up in inflation from around zero: this is now expected to get back to around 1% by the end of 2016 and not get to near 2% until the second half of 2017, though the forecasts in the Report itself were for an even slower rate of increase.
- However, more falls in the price of oil and imports from emerging countries in early 2016 will further delay the pick up in inflation. There is therefore considerable uncertainty around how quickly pay and CPI inflation will rise in the next few years and this makes it difficult to forecast when the MPC will decide to make a start on increasing Bank Rate.
- The weakening of UK GDP growth during 2015 and the deterioration of prospects in the international scene, especially for emerging market countries, have consequently led to forecasts for when the first increase in Bank Rate would occur being pushed back to quarter 4 of 2016. There is downside risk to this forecast i.e. it could be pushed further back.
- The UK are experiencing exceptional levels of volatility which are highly correlated to emerging market, geo-political and sovereign debt crisis developments.
- The downside risks to current forecasts for UK gilts yields and PWLB rates currently include:
    - Emerging country economies, currencies and corporates destabilised by falling commodity prices and or Fed. rate increases, causing a flight to safe havens (bonds).
    - Geopolitical risks in Eastern Europe, the Middle East and Asia, increasing safe haven flows.
    - UK economic growth and increases in inflation are weaker than are currently anticipated.
    - Weak growth or recession in the UK’s main trading partners – the EU and US.
    - A resurgence of the Eurozone sovereign debt crisis
    - Recapitalisation of European banks requiring move government financial support.
    - Monetary policy action failing to stimulate sustainable growth and combat the threat of deflation in western economies, especially in the Eurozone and Japan.
- The potential for upside risks to current forecasts for UK gilts yields and PWLB rates especially for longer term PWLB rates include:
    - Uncertainty around the risk of a UK exit from the EU.
    - The pace and timing of increases in the Fed. Funds rate causing a fundamental reassessment by investors of the

relative risks of holding bonds as opposed to equities and leading to a major flight from bonds to equities.

- UK inflation returning to significantly higher levels than in the wider EU and US, causing an increase in the inflation premium inherent to gilt yields.

4.4 Borrowing Strategy

4.4.1 The Council is currently maintaining an under-borrowed position, where CFR balance is greater than gross debt, see table 4.2. This is in line with the agreed strategy that the Council's cash balances be used to fund capital expenditure before additional borrowing is undertaken.

4.4.2 The MTFS is based on the following borrowing assumptions for the next ten years. However, the borrowing strategy is under constant review throughout the year as a result to changes in interest rates and borrowing opportunities. The proposed strategy for 2016/17 financial year is:

a) To consider the rescheduling (early redemption and replacement) of loans to maximise interest rate savings and possible redemption discounts.

b) If there was a significant risk of a sharp fall in long and short term rates e.g. due to a marked increase of risks around relapse into recession or of risks of deflation, then long term borrowings will be postponed, and potential rescheduling from fixed rate funding into short term borrowing will be considered.

c) If there was a significant risk of a much sharper rise in long and short term rates than currently forecast, perhaps rising from a greater than expected increase in world economic activity or a sudden increase in inflation risks, then the portfolio position will be re-appraised with the likely action that fixed rate funding will be drawn whilst interest rates were still relatively cheap.

d) Loans will primarily be arranged from the PWLB and other Local Authorities.

e) To maintain an appropriate balance between PWLB, Local Authority and other market debt in the debt portfolio and a balance in the maturity profile of debt.

f) To give full consideration to other debt instruments e.g. Local Authority Bonds as an alternative to PWLB borrowing. Due regard will be given to money laundering regulations. The Council is monitoring the development of the scheme and may participate if this proves beneficial.

4.4.3 There are three debt treasury indicators which ensure the activity of the treasury function remains within certain limits. This manages risk and reduces the impact of any adverse movement in interest rates. The indicators are:

- **Indicator 8** – Upper limit on fixed interest rate exposure. This identifies a maximum limit for fixed interest rates based upon the debt position net of investments. This has been set at 100% of the borrowing requirement.
- **Indicator 9** - Upper limit on variable rate exposure. This identifies a maximum limit for variable interest rates based upon the debt position net of investments. This has been set at 25% of the borrowing requirement.

Interest Rate Exposure (Upper Limits)	2014/15 Actuals £m	2015/16 Est. £m	2016/17 Est. £m	2017/18 Est. £m	2018/19 Est. £m	2019/20 Est. £m	2020/21 Est. £m	2021/22 Est. £m	2022/23 Est. £m	2023/2 Est. £m	2024/25 Est. £m	2025/26 Est. £m
(8) Limits on fixed interest rates based on net debt	*306.0*	665.6	796.6	796.1	745.2	686.2	677.5	676.6	674.3	677.1	680.8	682.2
% of fixed interest rate exposure	*100%*	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%	100%
(9) Limits on variable interest rates based on net debt	*0.0*	166.4	199.2	199.0	186.3	171.5	169.4	169.1	168.6	169.3	170.2	170.5
% of variable interest rate exposure	*25%*	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%	25%

- **Indicator 10 -** Maturity structure of borrowing. These gross limits are set to reduce the Council's exposure to large fixed rate sums falling due for refinancing.

(10) Maturity Structure of borrowing	Upper Limit
Under 12 months	40%
12 months to 2 years	40%
2 years to 5 years	80%
5 years to 10 years	80%
10 years and above	100%

4.5 Policy on Borrowing in Advance of Need (Future Capital Expenditure)

4.5.1 The Council will not borrow more than, or in advance of its needs, purely in order to profit from the investment of the extra sums borrowed. However, at any time the Council may obtain a loan or other financing at what are considered advantageous opportunities in anticipation of future capital expenditure, which can be invested temporarily. The Council may also borrow in the day to day management of its cash flow operations or as an alternative to redeeming higher yielding investments.

4.5.2 Any decision to borrow in advance of need will be within forward approved CFR estimates, and will be considered carefully to ensure value for money.

4.5.3 The Council will ensure there is a clear link between the capital programme across the future years and the maturity profile of the existing debt portfolio which supports the need to take funding in advance of capital expenditure.

4.5.4 The Council will ensure the ongoing revenue liabilities created, and the implications for the future plans and budgets have been considered and factored into the MTFS.

4.5.5 Consideration will be given to the alternative interest rate bases available, the most appropriate periods to fund and repayment profiles to use.

4.6 Debt Rescheduling on Existing Debt Portfolio

4.6.1 As short term borrowing rates will be considerably cheaper than longer term fixed interest rates there may be potential to generate savings by switching from the existing long term debt to short term debt. However, these savings will need to be considered in the light of the current treasury position and the size of the cost of debt repayment (premiums incurred). Debt rescheduling will only be carried out on current debt portfolio as future borrowing will be carried out as per this strategy and over shorter periods of time.

4.6.2 The reasons for rescheduling will include:

- the generation of cash savings and/or discounted cash flow savings;
- helping to fulfil the treasury strategy;
- enhance the balance of the debt portfolio.

4.6.3 All rescheduling will be reported to the Audit Committee at the earliest opportunity.

4.7 Annual Investment Strategy – Changes to Credit Rating Methodology

4.7.1 The main rating agencies (Fitch, Moody's and Standard & Poor's) have, through much of the financial crisis, provided some institutions with a ratings "uplift" due to implied levels of sovereign support. Commencing in 2015, in response to the evolving regulatory regime, all three agencies have begun removing these "uplifts" with the timing of the process determined by regulatory progress at the national level. The process has been part of a wider reassessment of methodologies by each of the rating agencies. In addition to the removal of implied support, new methodologies are now taking into account additional factors, such as regulatory capital levels. In some cases, these factors have "netted" each other off, to leave underlying ratings either unchanged or little changed. A consequence of these new methodologies is that they have also lowered the importance of the (Fitch) Support and Viability ratings and have seen the (Moody's) Financial Strength rating withdrawn by the agency.

4.7.2 In keeping with the agencies' new methodologies, the rating element of our own credit assessment process now focuses solely on the Short and Long Term ratings of an institution. While this is the same process that has always been used for Standard & Poor's, this has been a change in the use of Fitch and Moody's ratings. It is important to stress that the other key elements of the process, namely the assessment of Rating Watch and Outlook information as well as the Credit Default Swap (CDS) overlay have not been changed.

4.7.3 The evolving regulatory environment, in tandem with the rating agencies' new methodologies also means that sovereign ratings are now of lesser importance in the assessment process. The new regulatory environment is attempting to break the link between sovereign support and domestic financial institutions. This is in relation to the fact that the underlying domestic and where appropriate, international, economic and wider political and social background will still have an influence on the ratings of a financial institution.

4.7.4 It is important to stress that these rating agency changes do not reflect any changes in the underlying status or credit quality of the institution. They are merely reflective of a reassessment of rating agency methodologies in light of enacted and future expected changes to the regulatory environment in which financial institutions operate. While some banks have received lower credit ratings as a result of these changes, this does not mean that they are suddenly less credit worthy than they were formerly. Rather, in the majority of cases, this mainly reflects the fact that implied sovereign government support has effectively been withdrawn from banks. They are now expected to have sufficiently strong balance sheets to be able to withstand foreseeable adverse financial circumstances without government support. In fact, in many cases, the balance sheets of banks are now much more robust than they were before the 2008 financial crisis when they had higher ratings than now. However, this is not universally applicable, leaving some entities with modestly lower ratings than they had through much of the "support" phase of the financial crisis.

4.8 Annual Investment Policy

4.8.1 The Council's investment policy has regard to the CLG's Guidance on Local Government Investments ("the Guidance") and the 2011 revised CIPFA Treasury Management in Public Services Code of Practice and Cross Sectoral Guidance Notes ("the CIPFA TM Code").

4.8.2 The Council's investment priorities are the security of capital and the liquidity of investments. The Council will aim to achieve the optimum return on its investments commensurate with proper levels of security and liquidity.

4.8.3 Investment instruments identified for use in the financial year are listed in Appendix 1 under the 'Specified' and 'Non-Specified' Investment categories. Counterparty limits will be as set through the Council's Treasury Management Practices.

4.8.4 **Investment Counterparty Selection Criteria and Investment Strategy**

4.8.5 As the Council has run down its cash balances, surplus cash will be generated from cash flow movements e.g. a grant received in advance of spend or from borrowing in advance of need. Therefore investment activity will be kept to a minimum.

4.8.6 However, where it is necessary for investments to be undertaken in order to manage the Council's cash flows, the Council's primary principle is for the security of its investments. 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.
- 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.

4.8.7 The Corporate Director Resources 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.

4.8.8 The Councils minimum criteria will apply to the lowest available rating for any institution. For instance, if an institution is rated by the three credit agencies and two meet the Council's criteria and the other one does not, the institution will fall outside the lending criteria. This complies

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with a CIPFA Treasury Management Panel recommendation in March 2009 and the CIPFA Treasury Management Code of Practice.

4.8.9 In order to minimise the risk to investing, the Council has clearly stipulated the minimum acceptable credit quality of counterparties for inclusion on the lending list. The Council uses the creditworthiness service provided by Capita Asset Services which uses ratings from all three rating agencies, Fitch, Moody's and Standard and Poor's, as well as Credit Default Swap (CDS) spreads. Capita Asset Services monitors ratings on a real time basis and notifies clients immediately on any rating changes or possible downgrades.

4.8.10 All credit ratings will be monitored weekly. The Council is alerted to changes to ratings of all three rating agencies by Capita Asset Services.

- If a downgrade results in the counterparty or investment scheme no longer meeting the Council's minimum criteria it will be removed from the Council's lending list immediately.
- In addition to the use of credit ratings the Council will be advised of information in movement in CDS's against the iTraxx (brand name for the group of credit default swap index products) benchmark and other market data on a weekly basis. Extreme market movements may result in the downgrade of an institution or removal from the Councils lending list.

4.8.11 Sole reliance will not be placed on the use of Capita Asset Service's advice. The Council will also use market data, market information, information on government support for banks and the credit ratings of that government support.

4.8.12 The criteria for providing a pool of high quality investment counterparties (both Specified and Non-Specified investments), and is shown in the order of use by the Council, follows:

- UK Government (including gilts and the Debt Management Account Deposit Facility (DMADF)).
- Bank of Scotland call account (part of the Lloyds Banking Group).
- UK Local Authorities.
- All of the above would be subject to continuous credit rating reviews, specifically with regards to the credit rating methodology changes noted in 4.7.1.

4.8.13 Barclays Bank, the Council's own banker. If Barclays fall below the criterion in 4.8.12 then the following strategy will be followed:

- With regard to the three credit rating agencies, if one reduces its rating but the other two remain the same or improve, no action will be taken with regards to funds held with Barclays, ie maximum of £5m in the call account
- If two or more credit rating agencies reduce their ratings only, as the Council will still require to use the Barclays accounts for transactional purposes, a maximum balance of £500k will be left overnight to prevent the account becoming overdrawn and incurring overdraft fees
- Seek advice from Capita Asset Services
- The above action applies to Barclays only due to its status as the Council's banking provider. Use of other bank accounts would be subject to criteria set out in the point above.

The above approach has been developed following consideration of:

  - that the Council needs banking facilities to process

daily banking transactions, and such activity presents a lower risk profile compared to investment activity
    - the significant impact, resource requirement, and risk exposure of changing bank provider
    - the possible state and stability of the banking sector and viable alternative suppliers

- Local Authority Mortgage Scheme. Under this scheme the Council has placed funds of £2m with Lloyds Bank for a period of five years. This is classified as being an indemnity arrangement and therefore accounted for as a capital expenditure transaction, rather than a treasury management investment. Therefore LAMS is outside the Specified/Non specified categories but is included in this Strategy for completeness. Any other counterparty used will fall outside the Specified/Non specified categories as per the reason stated above. Therefore the minimum credit criteria need not apply to the LAMS scheme.

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- Banks Group 1 - Part nationalised UK banks - Lloyds Banking Group Plc. (Bank of Scotland and Lloyds) and Royal Bank of Scotland Group Plc. (National Westminster Bank, The Royal Bank of Scotland and Ulster Bank Ltd). These banks can be included if they continue to be part nationalised and / or they meet the ratings below.

- Banks Group 2 – good credit quality - the Council will only use banks which are UK banks and have the minimum credit ratings criteria relating to the type of investment being undertaken.

Agency	Short Term	Long Term
Fitch	F1	A
Moody's	P-1	Aa
Standard & Poor's	A-1	A

- Building Societies – if they meet the ratings above
- Money Market Funds - AAA rated
- Bill Payment Service – The Council currently has a contract with Santander UK who collect payments of Council Tax through the post office via various methods of payment such as Paypoint. The funds that are collected are transferred to the Council daily thus minimising the risk of Santander UK holding the Council's cash. This arrangement for the bill payment service falls outside the investment criteria for investments therefore any downgrade of Santander UK will not affect this service. However this arrangement will be closely monitored to ensure funds continue to be transferred daily.

4.8.14 The Council's lending list will comprise of the institutions that meet the investment criteria above. Each counterparty on the list is assigned a counterparty limit as per the table in Appendix 1. Counterparties that no longer meet the investment criteria due to a credit rating downgrade will be removed from the list and any changes will be approved by the Corporate Director: Resources. Approval will also be required if any new counterparties are added to the lending list.

4.8.15 Capita Asset Services approach to assessing creditworthiness of institutions is by combining credit ratings, credit watches, credit outlooks and CDS spreads to produce a colour coding system which the Council uses to determine the duration of investments. The Council will use counterparties within the following maximum maturity periods, in order to mitigate the risk of investing in these institutions:

Capita Asset Services Banding	**Description**

Capita Asset Services Banding	Description
Blue	1 year (only applies to nationalised / semi nationalised UK banks)
Orange	1 year
Red	6 months
Green	3 months
No colour	The Council will not invest with these institutions

4.8.16 The proposed criteria for Specified and Non-Specified investments are shown in Appendix 1 for approval. During this time of significant economic uncertainty due regard will be taken of the selection criteria outlined in 4.8.12, when using the options outlined in Appendix 1.

4.8.17 Investment returns expectations - Bank Base Rate is forecast to remain unchanged at 0.50% before starting to rise from quarter four in 2016. Bank Rate forecasts for financial year ends are:

Financial Year	Bank Base Rate	Forecast
2015/16	0.50%	There is an upside risk to these forecasts (i.e. if increases in Bank Rate occurs sooner than forecast) if economic growth remains strong and unemployment falls faster than expected. However there is also a downside risk if the pace of growth falls back particularly if the Bank of England inflation forecasts for the rate of unemployment prove to be too optimistic.
2016/17	0.63%	
2017/18	1.13%	
2018/19	1.63%	

4.8.18 **Indicator 11** - Upper limit for total principal sums invested for over 364 days. This limit is set with regard to the Council's liquidity requirements and to reduce the need for an early sale of an investment, and is based on the availability of funds after each year-end and up-dates are reported to the Audit Committee at midyear. These upper limits are to provide approved flexibility for future LAMS contributions.

(11) Interest Rate Exposure (Upper Limits)	2014/15 Actuals £m	2015/16 Est. £m	2016/17 Est. £m	2017/18 Est. £m	2018/19 Est. £m	2019/20 Est. £m	2020/21 Est. £m	2021/22 Est. £m	2022/23 Est. £m	2023/24 Est. £m	2024/25 Est. £m	2025/26 Est. £m

Principal sums invested > 364 days	*0.0*	0.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0	10.0

4.8.19 At the end of the year, the Council will report on its investment activity as part of its Annual Treasury Report to the Audit Committee.

4.8.20 The Corporate Director Resources may appoint external fund managers to access markets not available to the in-house treasury team, diversify the investment portfolio and to optimise investment income returns. Fund Managers will only be used if the Corporate Director Resources is satisfied the risk of loss is minimised and they can provide material out-performance when compared against comparative cash benchmarks. Fund Managers must comply with the Annual Investment Strategy.

4.9 Peterborough's Growth Delivery Project

4.9.1 The following model has been established and agreed in the paper submitted to Cabinet on the 24 February 2014 http://democracy.peterborough.gov.uk/documents/s19284/5.%20Funding%20Peterboroughs%20Future%20Growth.Pdf and the Executive Decision on the 9 December 2014 http://democracy.peterborough.gov.uk/ieDecisionDetails.aspx?ID=1022

4.9.2 A Joint Venture, Limited Liability Partnership (JV LLP) 50:50 owned and controlled by the Council and Lucent Peterborough Partnership SARL are working to create commercially viable Project Plans. Once an Project Plan is approved by the JV LLP board it will create a Special Purpose Vehicle (SPV) to oversee the plan implementation.

4.9.3 As projects are developed the Council will sell sites previously earmarked for disposal at their current market value to the JV LLP for development. The Council will receive Loan Notes from the JV LLP in consideration. The Council may also receive loan notes in consideration for any other costs it incurs on behalf the JV LLP.

4.10 Treasury Management Scheme of Delegation

4.10.1 The following is a list of the main tasks involved in treasury management and who in the Council is responsible for them:

Full Council / Audit Committee

- Receiving and reviewing reports on treasury management policies, practices and activities.
- Approval of Annual Strategy.

Audit Committee / S151 Officer (Corporate Director: Resources)

- Approval of / amendments to the Council's adopted clauses, Treasury Management Policy Statement and Treasury Management Practices.
- Budget consideration and approval.
- Approval of the division of responsibilities.
- Receiving and reviewing regular monitoring reports and acting on recommendations.

Section 151 Officer (Executive Director Resources) / Service Director Financial Services / Head of Corporate Finance

- Reviewing the Treasury Management Policy and

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procedures and making recommendations to the responsible body.

- Recommending clauses, treasury management policy/practices and making recommendations to the responsible body.
- Submitting regular treasury management reports.
- Submitting budgets and budget variations.
- Receiving and reviewing management information reports.
- Reviewing the performance of the treasury management function.
- Ensuring the adequacy of treasury management resources and skills, and the effective division of responsibilities within the treasury management function.
- Ensuring the adequacy of internal audit, and liaising with external audit.
- Recommending the appointment of external service advisors.

Specified and Non-Specified Investments **APPENDIX 1**

Specified Investment:

- Offer high perceived security such as placements with Central Government Agencies, Local Authorities or with organisations that have strong credit ratings
- They offer high liquidity i.e. short term or easy access to funds
- Are denominated in £ sterling
- Have maturity dates of no more than 1 year
- For an institution scheme to qualify as a ‘Specified Investment’ it must have a minimum rating (see 4.8.8)

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APPROVED "SPECIFIED" INVESTMENTS				
Investment Type	**Maximum Maturity period**	**Minimum Credit Criteria**	**Collective Limit £m**	**Individual Limit £m**
Debt Management Agency Deposit Facility	Currently only accepts deposits up to 6 months duration.	UK Government backed	N/A	75
Term deposits with UK Government & Local Authorities	6 months	Sovereign risk / high security although not credit rated	100	20
Term deposits & Certificates of Deposit with Banks Group 1	6 months	Minimum ratings - F1(Fitch - short term) AAA (long term)	100	15
UK Government & Local Authority Stock Issues	6 months	Sovereign risk / high security although not credit rated	100	20
Term deposits & Certificates of Deposit with Banks Group 2	6 months	Minimum ratings – F1 (Fitch-short term) A (long term)	50	10
Deposit accounts with regulated UK building societies	6 months	Minimum ratings - F1 (Fitch short term) A (long term)	50	10
Money Market Funds	Repayable on call, without notice.	Minimum rating – AAA (Fitch)	50	10
Commercial Paper (short term obligations	6 months	Minimum short term rating - F1 (Fitch)	10	10

APPROVED "SPECIFIED" INVESTMENTS				
Investment Type	**Maximum Maturity period**	**Minimum Credit Criteria**	**Collective Limit £m**	**Individual Limit £m**
issued by banks, corporations & other issuers).		(Held by custodian)		
Gilt & Bond Funds (open ended mutual funds investing in Gov. & corporate bonds)	Highly liquid, may be sold at any time.	Minimum rating - AAA-(Fitch, S&P A-1 etc.)	10	10
Reverse Gilt Repos (Gilts bought with commitment to sell on a specified date or on call, at agreed price)	6 months	UK Government backed (Held by custodian)	10	10
Treasury Bills	Maturities of up to 6 months Issued through a bidding process at a discount to face value	UK Government backed (Held by custodian)	10	10
Bonds issued by a financial institution guaranteed by UK Government	6 months	UK Government backed (Held by custodian)	10	10
Bonds issued by multilateral development banks	6 months	Minimum rating – AAA (Fitch, S&P A-1etc)	10	10

Non-Specified Investment:

- With the same institutions classified as “specified” investments but have maturity dates in excess of one year, or
- Are offered by organisations that are not credit rated or the credit rating does not meet the criteria set out above
- In the current economic climate the Council has run down its cash balances as an alternative to borrowing and investments have been made short term and the Council would not consider using investments that fall under the ‘Non-Specified’ Investments category at this time.

APPROVED "NON - SPECIFIED" INVESTMENTS				
Investment Type	**Repayable / Maturity Period**	**Minimum Credit Criteria**	**Collective Limit £m**	**Individual Limit £m**
Term deposits with UK Government & Local Authorities	Maturities of 1 - 5 years	Sovereign risk / high security although not credit rated	20	20
Term deposits & Certificates of Deposit with Banks Group 1	Maturities of 1 - 5 years Certificates of Deposit are tradable	Minimum ratings - F1(Fitch - short term) AAA (long term)	10	10
UK Government & Local Authority Stock Issues	Maturities of 1 - 10 years but tradable	Sovereign risk / high security although not credit rated	10	10
Term deposits & Certificates of Deposit with Banks Group 2	Maturities of 1 - 5 years Certificates of Deposit are tradable	Minimum ratings – F1 (Fitch-short term) A (long term)	20	10
Deposit accounts with regulated UK building societies	Maturities of 1 – 5 years	Minimum ratings - F1 (Fitch short term) A (long term)	5	5
Foreign Government Stock Issues (priced in £ Sterling)	Maturities of 1 - 10 years but tradable	Minimum rating – AAA (Fitch, S&P A-1etc) (Held by custodian)	5	5
Term deposits with UK building societies without formal credit ratings	Maturities of up to 1 year	Financial position assessed by Corporate Director: Resources	5	5
Bonds issued by a financial institution guaranteed by UK Government	Maturities of 1 - 10 years but tradable	UK Government backed Minimum rating – AAA (Fitch, S&P etc.)	5	5

APPROVED "NON - SPECIFIED" INVESTMENTS				
Investment Type	**Repayable / Maturity Period**	**Minimum Credit Criteria**	**Collective Limit £m**	**Individual Limit £m**
Bonds issued by multilateral development banks	Maturities of 1 - 10 years but tradable	Minimum rating - AAA (Fitch, S&P A-1etc)	5	5
Floating Rate Notes (fixed term but interest rate varies quarterly)	Maturities of 1 - 5 years but tradable	Financial position assessed by Corporate Director: Resources. Requires capital or revenue financing as share or loan capital.	5	5
Bonds issued by corporate issuers other than sovereign bonds	Maturities of 1 - 10 years but tradable	Minimum rating – AAA (Fitch, S&P A-1etc) Requires capital or revenue financing as share or loan capital	5	5

Explanation Of Credit Ratings

APPENDIX 2

Agency	Short Term	Long Term
Fitch	**F1**-Highest short-term credit quality. Indicates the strongest intrinsic capacity for timely payment of financial commitments; a "+" may be added to denote any exceptionally strong credit feature.	**A**-High credit quality. 'A' ratings denote expectations of low credit risk. The capacity for payment of financial commitments is considered strong. This capacity may, nevertheless, be more vulnerable to adverse business or economic conditions than is the case for higher ratings.
Moody's	**P-1**-superior ability to repay short-term debt obligations	**Aa**-high quality and are subject to very low credit risk
Standard & Poor's	**A-1**-The obligor's capacity to meet its financial commitment on the obligation is strong. Within this category, certain obligations are designated with a plus sign (+). This indicates that the obligor's capacity to meet its financial commitment on these obligations is extremely strong.	**A**-more susceptible to the adverse effects of changes in circumstances and economic conditions. However the obligor's capacity to meet its financial commitment on the obligation is still strong.

APPENDIX 3

Minimum Revenue Provision (MRP) – Consideration of Four Further Amendments to the MRP Calculation

Context

1. A comprehensive review of the Council's method for calculating its Minimum Revenue Provision (MRP) has been undertaken in order to ensure that the amount of revenue represents a fair charge, compared to the life of the asset that is being financed via borrowing.
2. A paper considering an amendment to 'historic and supported borrowing MRP calculation' was considered as part of the Phase 1 budget proposals. This option looked at changing the length of the repayment of this element of borrowing from the budgeted 25 years to 42 years, on an equal instalment method. The basis for this change is to match the repayment of borrowing to the economic usefulness of the asset, see point 6 to 8 below.
3. This paper presents further review of the MRP charge from those agreed in the Phase 1 proposals, with consideration given to additional amendments to the calculation with regards to:
    a. Historic and Supported Borrowing – using the annuity method. The Phase 1 proposal is based on the equal instalment method. The annuity method factors in the time value of money – ie a £ is worth more now than in the future, see point 9.
    b. Current MRP profile for the 2007/08 & 2008/09 capital expenditure – from equal instalments to annuity method of calculation. Following on from a review of MRP undertaken in 2009/10, there are two years of capital expenditure where equal instalments is applied, as this amendment was applied to new capital expenditure only at the time, see points 16 to 19.
    c. The timing of MRP for the Private Finance Initiative (PFI) related assets – matching the MRP charge to the asset life using the annuity method, rather than the current derived calculated approach, see points 21 to 23.
    d. The use of Capital Receipts – amendment to the Council's MRP policy so that capital receipts are used as part of a contribution to the MRP charge, rather than netting down the total amount of borrowing required, see points 26 to 29.
4. The above amendments would result in the Council having one consistent method for calculating its MRP for all borrowing which has been undertaken to support capital investment in the city. This is the annuity method based on asset lives rather than the myriad of methods used presently, see Appendix Four for a summary. The Council has been using the annuity method as the basis for its MRP charge since 1 April 2010.

What is Minimum Revenue Provision (MRP)

5. The Council can borrow to fund its capital programme. The cost of borrowing impacts on the annual revenue budget, in two ways, through:
    - Interest payments on the loan
    - Amounts set aside for the repayment of the loan – known as Minimum Revenue Provision (MRP) i.e. the principal element of the loan

    Statute allows the Council to choose the calculation methodology of its MRP as long as it is prudent. It is recommended that aligning this charge to the life of assets, on an annuity method basis, represents the best value approach for tax payers, now and in the future.

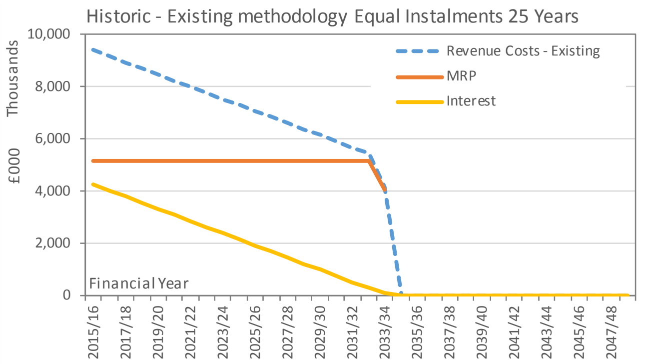
Amendment to the Historic Borrowing and Supported Borrowing

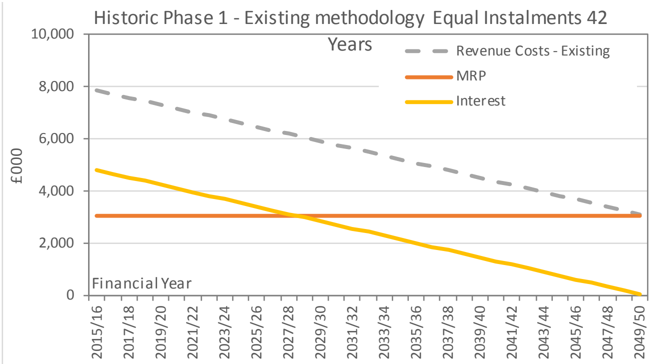
6. Like many authorities the Council has continued to apply the previous regulatory approach, calculating MRP at 4% for the capital expenditure incurred prior to 1 April 2007 which was funded by borrowing, and for supported borrowing undertaken from 2007/08 to 2010/11. However, there is increasing acceptance that the MRP charged for this historic and supported debt should more correctly be linked to the average useful life of the assets involved. The current regulatory approach (a percentage basis) does not reflect this view. Currently, 4% of the balance of historic debt at 1 April 2007 is provided for out of the revenue budget as MRP which the Council has budgeted to be repaid over 25 years.

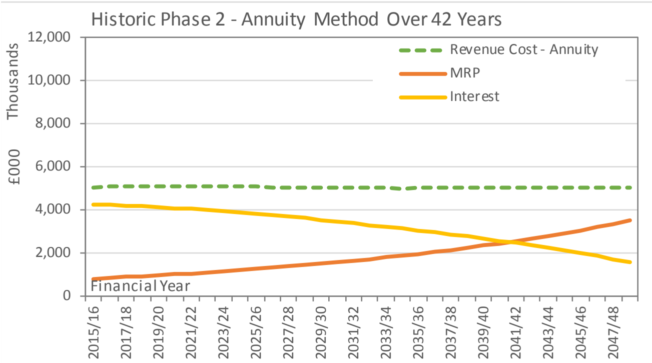
7. Linking MRP to the average useful life of an asset is in keeping with the general principle of achieving a prudent approach set out in the DCLG guidance that the profile of MRP charges should reflect the economic benefit the Council gets from using the asset to deliver services over its useful life. This ensures that Council Tax payers are being charged each year in line with asset usage and prevents current taxpayers meeting the cost of future usage or future tax payers being burdened with “debt” relating to assets that are no longer in use.

8. A fairer way of matching the MRP charge to Council Tax payers with the use of the assets is to revise the repayment period to 42 years, which is the weighted average life of the Council’s assets. This is based on the fact the Council’s asset base has not materially changed during the time since 1 April 2007. This equates to a rate of 2.38% compared to the historic 4%. Any saving on annual MRP charge however, is partially offset by an increased interest cost due to paying the debt off over a longer period.

9. It would also be fairer if the MRP charge were to factor in the time value of money in the future. This adjustment would ensure that Council Tax payers of the future pay an amount for the use of the assets, which would be comparable in real terms to that being paid by current Council Tax payers. This can be achieved by adopting an annuity basis for calculating the annual MRP charge. The Council has been using the annuity method as the basis for its MRP charge since 1 April 2010.







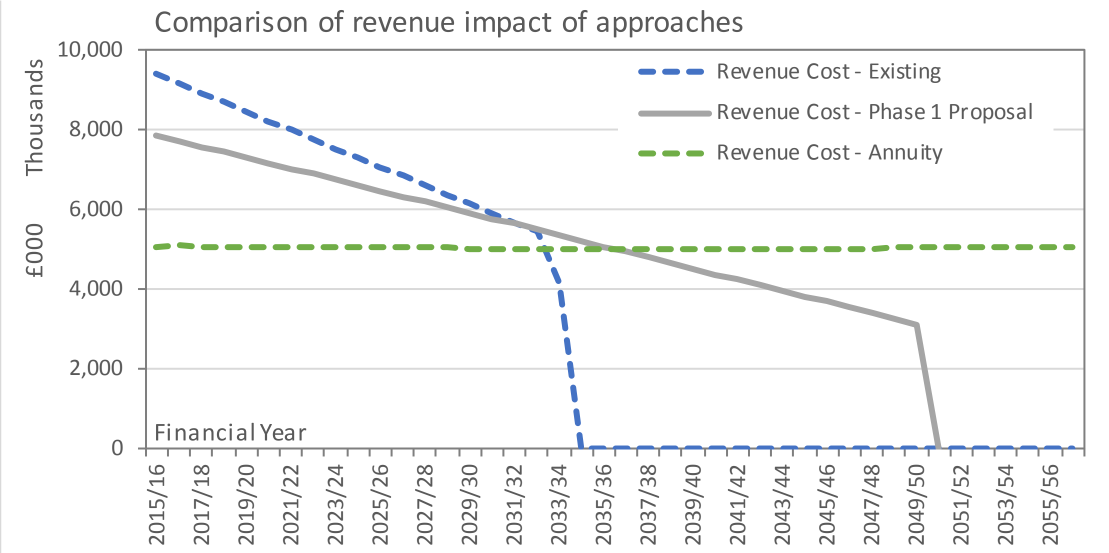
10. The following charts illustrate the proposed changes discussed in points 6 to 9 above.

11. To assess the options over the different time periods, of 25 and 42 years, the impact of time is factored into the analysis of the revenue impact via the 'net present value' (NPV) calculation at 3% - this is the rate recommended by the Treasury's 'Green Book'. Taking into account interest payments, the NPV of this borrowing shown in the following table:

	MRP £000	**Interest £000**	**Total Revenue £000**	**NPV £000**
Currently budgeted	96,683	41,083	137,766	110,200
Proposed amendment	96,683	115,057	211,740	123,159
Difference	**0**	**73,974**	**73,974**	**12,959**

12. The differences are a result of the change in the split of interest and principal elements of the debt payments. Compared to the 4% method, the revised method results in the principal being paid over a longer time period, which results in greater interest payments overall.

13. A comparison of the revenue impact of the current method, moving to 42 years equal instalment, and then the final proposed method of 42 years using the annuity rate is



provided below.

14. It is important to stress that the change in methodology eliminates the inequality created by the accelerated charging basis of the Regulatory Method. The proposed basis is fairer giving a more proportionate profile charge based on asset usage over the whole asset lives.

15. Expected benefit from this amendment is shown the following table:

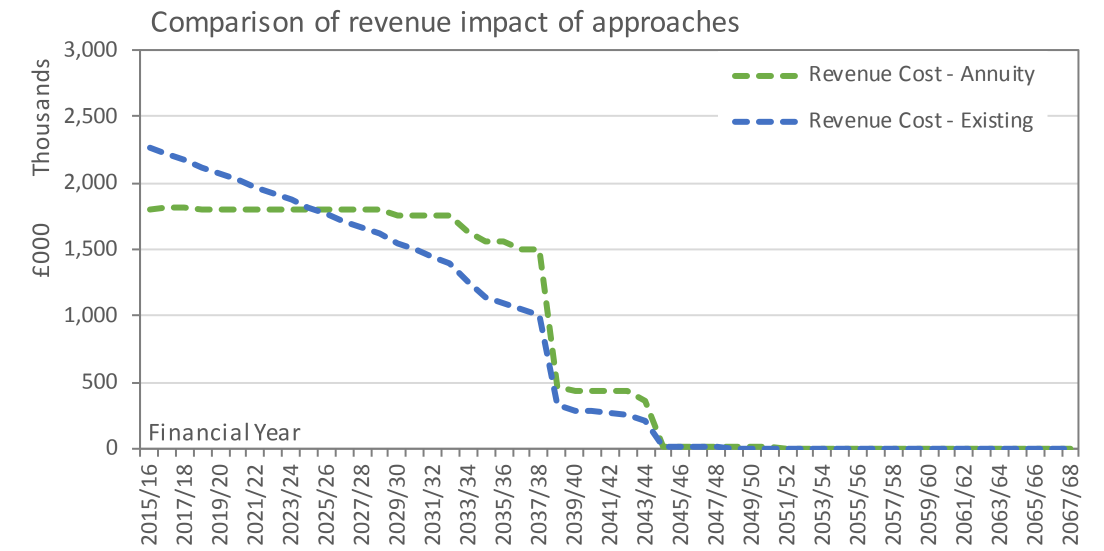
	2015/16 £000	**2016/17 £000**	**2017/18 £000**	**2018/19 £000**	**2019/20 £000**	**2020/21 £000**
MRP	(4,343)	(4,306)	(4,268)	(4,228)	(4,186)	(4,143)
Interest	0	232	408	594	789	982
Net Benefit	**(4,343)**	**(4,074)**	**(3,860)**	**(3,634)**	**(3,397)**	**(3,161)**

Amendment to the Current MRP Profile for 2007/08 & 2008/09 Capital Expenditure

16. In 2009/10 the Council undertook a MRP review which led to the change in MRP calculation methodology, from equal instalments to the annuity method. This was applied prospectively, which has meant that there are two years, 2007/08 and 2008/09, where the equal instalment methodology is still applied.

17. In line with the arguments set out above work has been undertaken to review the impact of changing these two years of borrowing from a repayment based on equal instalments to the annuity method.

18. The following chart shows how the overall revenue impact changes for this second element.



19. Expected benefit from this amendment is shown the following table:

	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000	2020/21 £000
MRP	(464)	(435)	(404)	(372)	(339)	(304)
Interest	0	26	41	59	75	90
Net Benefit	**(464)**	**(409)**	**(363)**	**(313)**	**(264)**	**(214)**

20. To assess the options over the different time periods, the impact of time is factored into the analysis of the revenue impact via the 'net present value' (NPV) calculation at 3% - this is the rate recommended by the Treasury's 'Green Book'. Taking into account interest payments, the NPV of this borrowing shown in the following table:

	MRP £000	Interest £000	Total Revenue £000	NPV £000
Currently budgeted	26,169	14,236	40,404	30,535
Proposed amendment	26,169	16,640	42,809	31,038
Difference	**0**	**2,405**	**2,405**	**503**

Amendment to the timing of MRP for the PFI related assets

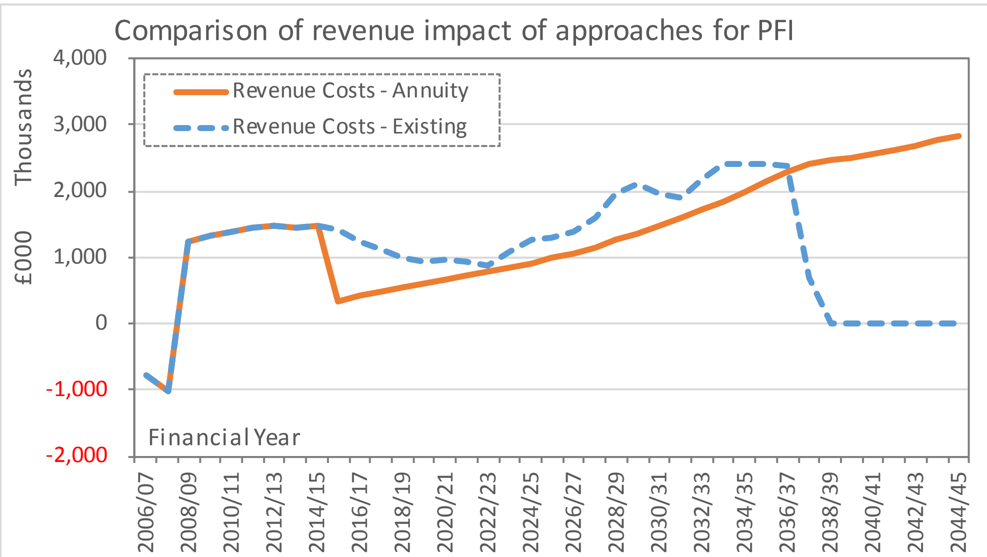
21. As part of the Council's conversion to International Financial Reporting Standards (IFRS), for the 2009/10 financial year the Council was required to change its accounting policy with regards to the secondary school Private Finance Initiative (PFI). As with other PFI schemes across the country, the Council had previously accounted for this transaction as an 'off balance sheet' item, and thus the cost of the scheme was charged against revenue funds only. The change in accounting policy meant that the Council had to recognise this scheme in terms of fixed assets (the school buildings) along with the equivalent long term liability to repay the loan from the private financer, both of which are now carried on the balance sheet.

22. As a result of the above change, this scheme is now accounted for as a capital transaction, and in order to repay the private finance liability an MRP charge has been derived from the initial PFI model. In order for the changes in accounting policy to have no overall impact on the Council's revenue funds, it was agreed by CIPFA, for schemes in existence prior to 2009/10 that the MRP charge would be the difference that remained from taking the interest charge and service costs from the unitary charge, see example below.

	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000	2020/21 £000
PFI Unitary Charge	8,041	8,124	8,209	8,295	8,385	8,476
Less Interest Charge	2,731	2,544	2,390	2,211	2,071	1,994
Less Service Cost	3,902	4,347	4,714	5,096	5,390	5,508
Resultant MRP	**1,408**	**1,233**	**1,105**	**988**	**924**	**974**

This means that depending on the life cycle costs built into the PFI model, the MRP is not uniform through the course of the scheme.

23. Following the wider review of the Council's MRP charge it has been found that some Councils are proposing to amend the timing of the MRP charge linked to PFI schemes by matching the charge to the life of the asset, rather than the life of the contract which is currently the case. Thus de-coupling the MRP calculation from the original PFI model, the impact of this would be to extend the period of debt repayment by nine years. As the period changes the Council would also need to apply a different mechanism for calculating the MRP charge, rather than the balancing amount outline in point 22 above, and to be



consistent with all other MRP charges the annuity method is proposed. The following chart illustrates this proposal:

24. Expected benefit from this amendment is shown the following table:

	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000	2020/21 £000
MRP	(1,058)	(858)	(711)	(556)	(458)	(475)
Interest	0	51	96	125	149	171
Net Benefit	**(1,058)**	**(807)**	**(615)**	**(431)**	**(309)**	**(304)**

25. To assess the options over the different time periods, the impact of time is factored into the analysis of the revenue impact via the 'net present value' (NPV) calculation at 3% - this is the rate recommended by the Treasury's 'Green Book'. Taking into account interest payments, the NPV of this borrowing shown in the following table:

	MRP £000	Interest £000	Total Revenue £000	NPV £000
Currently budgeted	35,530	33,499	69,029	27,080
Proposed amendment	35,530	44,100	79,631	33,513
Difference	**0**	**10,602**	**10,602**	**6,434**

Amendment to the use of Capital Receipts

26. Subject to these MRP amendments being agreed at the relevant MTFS budget groups, the Council's MRP policy, as contained in the MTFS, will need to be updated and achieve Council approval before the adjustments can take place.

27. A further amendment which is proposed to the MRP policy is in regards to the use of capital receipts to offset the MRP charge in year, rather than using capital receipts to offset the total amount of borrowing undertaken in year. The following table illustrates this approach using 2014/15 data.

	2014/15	
	Approach Now £000	Proposed £000
Capital Expenditure	107,047	107,047
Capital Grants	(35,561)	(35,561)
Amount funded from borrowing	70,486	70,486
Capital receipts	(2,906)	-
Borrowing on which to base MRP calculation	67,581	70,486
MRP	(10,916)	(8,012)
MRP - from capital receipts	-	(2,906)
Overall increase in borrowing for the year	57,665	59,570

28. As can be seen in the previous table, under the new proposed approach the total amount that borrowing is repaid is the same at £10,916k, but rather than it being funded wholly from revenue budgets, an element is funded via capital receipts income. This amendment better reflects the cash transactions of repaying debt.

29. This approach also increases the amount of borrowing undertaken as the capital receipt offsets the MRP made from revenue funds, rather than offsetting the total amounts of borrowing required on which MRP is charged.

30. The following table shows the MTFS capital receipt profile, and the associated additional borrowing costs of this proposed amendment. It should be noted that timing and amount of receipt may vary.

	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000
Capital receipt per MTFS (less LAMS)	11,820	2,215	5,525	145	-
Additional Interest Costs	139	625	702	714	720
Capital receipt used to repay debt per disposal paper	(5,341)	(3,100)	(2,610)	(1,100)	(460)
Net Impact on Revenue	**(5,202)**	**(2,475)**	**(1,908)**	**(386)**	**260**

31. As part of the recent Spending Review announcements, the Department of Communities & Local Government (DCLG) launched 'Draft Guidance on the Flexible Use of Capital Receipts' for consultation. This proposal would enable the Council to use capital receipts on the revenue costs of reform projects until 31 March 2019.

32. This option has not been included in the following summary of savings, but rather reflects an option to amend the MRP policy that Council approves at each MTFS so that this flexibility is available to the Council and its use determined on a year by year basis.

Summary and next steps

33. The following table provides a summary of the savings proposed in this paper (excludes capital receipts proposal). It is based on the assumption that the amendment to the calculation of MRP occurs prospectively from 2015/16.

MRP adjustment	**2015/16 £000**	**2016/17 £000**	**2017/18 £000**	**2018/19 £000**	**2019/20 £000**	**2020/21 £000**
Historic	(4,343)	(4,306)	(4,268)	(4,228)	(4,186)	(4,143)
2007/08 & 2008/09	(464)	(435)	(404)	(372)	(339)	(304)
PFI Adjustment	(1,058)	(858)	(711)	(556)	(458)	(475)
Phase 2 MRP Adjustment	**(5,865)**	**(5,599)**	**(5,383)**	**(5,156)**	**(4,983)**	**(4,922)**
Additional Interest Estimate						
Historic	0	231	407	593	788	981
2007/08 & 2008/09	0	26	41	58	75	90
PFI Adjustment	0	50	96	125	149	170
Phase 2 Interest Subtotal	**0**	**307**	**544**	**776**	**1,012**	**1,241**
Net Impact for Phase 2	**(5,865)**	**(5,292)**	**(4,839)**	**(4,380)**	**(3,971)**	**(3,681)**
Savings already included as part of Phase 1	2,000	2,000	2,000	2,000	2,000	2,000
Additional benefit	**(3,865)**	**(3,292)**	**(2,839)**	**(2,380)**	**(1,971)**	**(1,681)**

34. The Council has undertaken a review of the application of these MRP adjustment with other local authorities, and precedence exists for all the adjustments considered in this paper. However, it should be noted that these MRP policy amendment proposals are currently being discussed with the Council's external auditors with initial feedback provided on 5 January which this paper reflects. Final review by the Council's auditors is ongoing which includes examination of the time period put forward by the Council of 42 years. Should an alternative time period be recommended this will be agreed by the

Corporate Director Resources in liaison with external audit. This will help ensure that they are not 'minded to challenge' these adjustments in the future.

35. Further items to note:

- For capital projects funded from the 'Invest To Save' budget, savings generated from these schemes should still be used to offset the MRP charge.
- The numbers used in this paper are based on best estimates on the knowledge at this time. The actual final numbers will vary due to the profiling of expenditure of the capital programme, timing of asset disposals, and prevailing interest rates at the time of borrowing.

36. The following table illustrates the impact of the proposed amendments on the MRP budget.

MRP adjustment	2015/16 £000	2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000	2020/21 £000
MTFS MRP Budget	**12,094**	**14,630**	**15,144**	**14,678**	**14,945**	**15,121**
Historic	(4,343)	(4,306)	(4,268)	(4,228)	(4,186)	(4,143)
2007/08 & 2008/09	(464)	(435)	(404)	(372)	(339)	(304)
PFI Adjustment	(1,058)	(858)	(711)	(556)	(458)	(475)
Phase 2 MRP Adjustment	**(5,865)**	**(5,599)**	**(5,383)**	**(5,156)**	**(4,983)**	**(4,922)**
Revised MRP Budget	**6,229**	**9,031**	**9,761**	**9,522**	**9,962**	**10,199**
MRP Charge funded by:						
Capital Receipts Substitution	5,341	3,100	2,610	1,100	460	0
Revenue	888	5,931	7,151	8,422	9,502	10,199
Revised MRP Budget	**6,229**	**9,031**	**9,761**	**9,522**	**9,962**	**10,199**

37. The following table summarises all of the proposed amendments over the various time periods involved. As per earlier tables the impact of time has been factored into the analysis of the revenue impact via the 'net present value' (NPV) calculation at 3% - this is the rate recommended by the Treasury's 'Green Book'.

Type of Debt		MRP £000	Interest £000	Total Revenue £000	NPV £000
Historic	Currently budgeted	96,683	41,083	**137,766**	110,200
	Proposed amendment	96,683	115,057	**211,740**	123,159
	Difference	**0**	**73,974**	**73,974**	**12,959**
2007/08 & 2008/09	Currently budgeted	26,169	14,236	**40,404**	30,535
	Proposed amendment	26,169	16,640	**42,809**	31,038
	Difference	**0**	**2,405**	**2,405**	**503**
PFI Adjustment	Currently budgeted	35,530	33,499	**69,029**	27,080
	Proposed amendment	35,530	44,100	**79,631**	33,513
	Difference	**0**	**10,602**	**10,602**	**6,434**
TOTAL	Currently budgeted	158,382	88,817	**247,199**	167,815
	Proposed amendment	158,382	175,798	**334,180**	187,710
	Difference	**0**	**86,980**	**86,980**	**19,895**

Appendix Four – Summary of the MRP Current Calculation Methodologies, Impact of Amendments for 2015/16 & Overprovided Amounts

Age of Debt	Current method	Change considered	Debt Amount Outstanding @ 31.03.2015	Gross Debt MRP Calc. on	Current Est. MRP Charge for 2015/16	Proposed MRP Charge for 2015/16
Pre 2007/08 debt (ie debt up to 31.03.2007)	Charged at historic 4%	Change the length over which the debt is paid – from budgeted 25 years (4%) to 42 years (2.38% - based on the actual weighted average of the Councils assets, so a direct link to asset base)	79,669,509	110,652,095	5,144,902	802,574
		Using the 2.38% in an annuity calculation rather than an equal instalment or reducing balance method				
Supported Borrowing post 2007/08		As per above points - this debt is currently calculated on the same 4% basis	17,013,581	25,756,256		
Unsupported borrowing 2007/08 & 2008/09	Charged in relation to asset life on equal instalment method	There are two years of debt that are calculated using the old equal instalment method. The Council moved from this methodology in 2009/10. Proposal to amend these elements of the calculation so that repayment of this debt to be based on annuity method also.	26,407,492	33,542,041	1,114,773	651,277
Unsupported borrowing Post 2008/09	Charged in relation to asset life on annuity method	Continue to use existing annuity methodology based on actual life of asset to which borrowing has been taken for (this is net of Invest To Save schemes).	258,906,033	265,280,581	3,870,545	3,870,545
Private Finance Initiative (PFI) - Finance Lease	Charged derived from using the PFI model	Change the length over which the debt is paid from 30 years as per contract life to 39 years per asset life. As part of this change in life apply on an annuity method calculation.	35,530,480	43,586,532	1,407,854	349,918
Other Finance Leases	Charged in relation to asset life on annuity method	Continue to use existing annuity methodology based on actual life of asset to which borrowing has been taken for.	4,885,719	11,149,818	556,240	556,240
			422,412,813	**489,967,324**	**12,094,314**	**6,230,554**