

CYNGOR SIR POWYS COUNTY COUNCIL.

**AUDIT COMMITTEE
To be emailed**

**CABINET
12th February 2019**

**REPORT AUTHOR: County Councillor Aled Davies
Portfolio Holder for Finance**

SUBJECT: Treasury Management Qtr 3 Report

REPORT FOR: Information

1. Summary

- 1.1 CIPFA's 2009 Treasury Management Bulletin suggested:
"In order to enshrine best practice it is suggested that authorities report formally on treasury management activities at least twice a year and preferably quarterly."

The CIPFA Code of Practice on Treasury Management emphasises a number of key areas including the following:-

- xi. Treasury management performance and policy setting should be subject to scrutiny prior to implementation.

- 1.2 In line with the above, this report is providing information on the activities for the quarter ending 31st December 2018.

2. Economic Background and Forecasts

- 2.1 The economic background is attached at Appendix B.
- 2.2 The most recent forecast of interest rates by the Authority's advisor is as follows:

	Mar 19	Jun 19	Sep 19	Dec 19	Mar 20	Jun 20	Sep 20	Dec 20
Bank rate	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%
5yr PWLB	2.10%	2.20%	2.20%	2.30%	2.30%	2.40%	2.50%	2.50%
10yr PWLB	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%	2.90%	3.00%
25yr PWLB	2.90%	3.00%	3.10%	3.10%	3.20%	3.30%	3.30%	3.40%
50yr PWLB	2.70%	2.80%	2.90%	2.90%	3.00%	3.10%	3.10%	3.20%

3. Treasury Management Strategy

- 3.1 The Treasury Management Strategy approved by Full Council on 8th March 2018 is at Appendix A.
- 3.2 The Authority's investment priorities within the Strategy are: -

- (a) the security of capital and
- (b) the liquidity of its investments.

3.3 The Authority aims to achieve the optimum return on its investments commensurate with proper levels of security and liquidity. The risk appetite has been low in order to give priority to security of investments.

4. Current Investments

4.1 The current investment market is difficult in respect of earning the level of interest rates commonly seen in previous years as rates are very low and in line with the 0.75% Bank Rate.

4.2 The Authority had no investments at 31st December 2018.

4.3 Higher return rates are difficult to achieve as the Authority is not in a position to invest its cash for more than a short period of time.

4.4 Redemption Penalties:
There are no current fixed investments to redeem.

4.5 Investment returns in future years:
Our advisors' current suggested earning rates for investments for budgeting purposes are as follows:-

2018/19	0.75%
2019/20	1.00%

These are based on investments for up to three months duration.

5. Credit Rating Changes

5.1 There have been no credit rating changes relevant to this Authority's position during the last quarter.

5.2 The credit rating list for end of December is attached as a separate file to this report.

6. Borrowing / Re-scheduling

6.1 Effective management of the Authority's debt is essential to ensure that the impact of interest payable is minimised against our revenue accounts whilst maintaining prudent borrowing policies.

6.2 The Authority's Capital Position:

The Council's underlying need to borrow for capital expenditure is termed the Capital Financing Requirement (CFR). This figure is a gauge of the Council's indebtedness. The CFR results from the capital activity of the Council and resources used to pay for the capital spend. It represents the current year's unfinanced capital expenditure and prior years' net or unfinanced capital expenditure which has not yet been paid for by revenue or other resources.

Part of the Council's treasury activities is to address the funding requirements for this borrowing need. Depending on the capital expenditure programme, the treasury service organises the Council's cash position to ensure that sufficient cash is available to meet the capital plans and cash flow requirements. This may be sourced through external borrowing or utilising temporary cash resources within the Council.

Net external borrowing (borrowings less investments) should not, except in the short term, exceed the total of CFR in the preceding year plus the estimates of any additional CFR for the current year and next two financial years. This allows some flexibility for limited early borrowing for future years.

Original CFR Position:

	As at 31.03.18 Actual	2018/19 Original Estimate	2019/20 Original Estimate	2020/21 Original Estimate
	£M	£M	£M	£M
Capital Financing Requirement	318,036	382,916	416,618	434,710

Updated CFR position as at 31.12.18:

	As at 31.03.18 Actual	2018/19 Current Estimate	2019/20 Current Estimate	2020/21 Current Estimate
	£M	£M	£M	£M
Capital Financing Requirement	324,480	372,193	412,448	425,966

- 6.3 The Authority had outstanding long-term external debt of £251.4M at 31st March 2018. In relation to the CFR figure for 31st March 2018, this equated to the Authority being under borrowed by £73.1M. Using cash reserves as opposed to borrowing has been a prudent and cost effective approach over the last few years. However, members will be aware that internal borrowing is only a temporary situation and officers have advised that, based on capital estimates, it would be necessary for the Authority to borrow at stages over the next few years.

In line with this, £37.9M of longer-term borrowing has taken place in the current financial year with borrowing of a further £30m-£40m anticipated before financial year end.

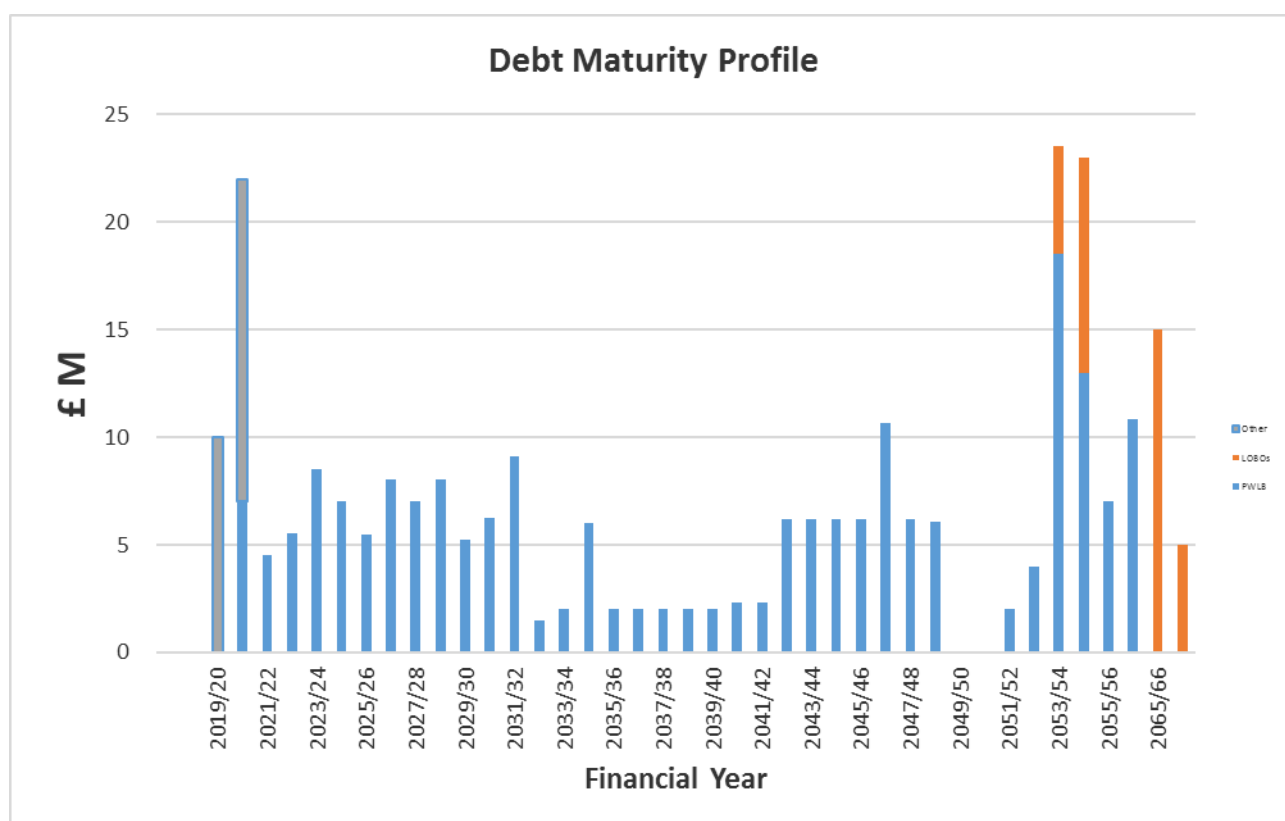
- 6.4 LOBO Loan:
Officers continue to be proactive in managing the Authority's debt portfolio. In November we were contacted by the lender of one of our LOBO loans. The lender intended to sell the loan (which is not an uncommon practice) but were offering us the opportunity to bid for it ourselves. As such, and following discussions with our advisors, we submitted a bid which was successful. Although this buy-out incurred a premium cost, it resulted in an overall revenue saving over the remaining 30 year period of the loan as the interest saved is greater than the premium cost. This was a good outcome for the Authority.

6.5 Capital Budget/Spend per efinancials:

Capital:	Approved Budget £	Working Budget £	Actual Capital Spend (not including commitments) £	%age spend
	85,725,189			
June		124,856,235	6,518,210	5.22%
Sept		126,377,477	25,547,244	20.20%
Dec		120,156,720	45,531,273	37.89%

The financing of the approved capital budget included £17.9M of Prudential borrowing in total.

6.6 Debt Maturity Profile as at 31.12.18:



6.7 PWLB Loans Rescheduling:

The Public Works Loans Board released a circular regarding rates on 20th October 2010. As a result of this, rates immediately increased by 0.87-0.88 basis points across the board. The overall impact of this circular was that it is far more difficult for authorities to reschedule debt. PWLB interest rates in the last quarter have not been conducive towards any rescheduling.

7. Prudential Indicators

7.1 All TM Prudential Indicators were complied with in the quarter ending 31st December 2018.

8. VAT

8.1 The Technical Section of Finance act as the authority's VAT section. VAT can pose a risk to the authority hence the TM has been asked to include VAT information in these quarterly reports.

8.2 The monthly VAT returns were submitted within the required deadlines during the quarter ending 31st December 2018.

8.3 Key Performance Indicators:

The VAT KPI's for 2018/19 are attached at Appendix C.

Proposal

It is proposed that the Treasury Management quarterly report is received.

Statutory Officers

The Head of Financial Services (acting s151 officer) notes the content of the report and supports the recommendation.

The Solicitor to the Council (Monitoring Officer) has made the following comment: "I have nothing to add to the report".

Future Status of the Report

Not applicable

Recommendation:		Reason for Recommendation:	
That the Treasury Management Quarterly Report be received		To ensure Cabinet remains informed about current Treasury Management performance	
Relevant Policy (ies):		Treasury Management Policy	
Within Policy:	Y	Within Budget:	N/A
Person(s) To Implement Decision:		N/A	
Date By When Decision To Be Implemented:		N/A	
Contact Officer Name:	Tel:	Fax:	Email:
Ann Owen	01597 826327	01597 826290	ann.owen@powys.gov.uk

Background Papers used to prepare Report:

CIPFA Code of Practice on Treasury Management and Cross Sectoral Guidance Notes
Treasury Management Policy Statement
Advisors' Information
WAG Guidance on Local Government Investments 2010
PWLB circulars

Appendix A:

Approved Treasury Management Strategy 2018/19:

7.5 “High” credit quality:

7.5.1 It is proposed that the Authority continue with the following in respect of defining a “high” credit quality. If a rating is not available from any of the rating agencies then the available ratings will be used. Members will note that this proposal excludes investments with some banks off the advisors’ suggested list:-

Long Term Ratings (in respect of long-term investments):

Permitted Fitch Ratings	Permitted Moodys Ratings	Permitted S&P Ratings
AAA	Aaa	AAA
AA+	Aa1	AA+
AA	Aa2	AA
AA-	Aa3	AA-

Short Term Ratings (in respect of short-term investments):

Permitted Fitch Ratings	Permitted Moodys Ratings	Permitted S&P Ratings
F1+	N/A	A-1+
F1	P-1	A-1

7.6 Country limits:

7.6.1 It is proposed that the Authority will use approved counterparties from the UK and approved counterparties from other countries with the following sovereign credit ratings:-

Permitted Fitch Ratings	Permitted Moodys Ratings	Permitted S&P Ratings
AAA	Aaa	AAA

Country	Maximum Investment per Country	Credit Rating/Other Assessment of Risk
AAA countries	£20M (held in call accounts)	As per rating list
UK	No Maximum Investment	As per rating list

7.7 Group/Institutions - Counterparty Criteria/Limits:

Specified Investments:

Institution	Maximum Investment per Group/Institution £M	Maximum Length	Credit Rating/Other Assessment of Risk
UK Banks	20 (a maximum £10M to be held in fixed term investments)	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	5	Up to 364 days	As per Link's matrices and the Authority's definition of a high credit rating
Other Local Authorities	25	Up to 364 days	N/A

Non-Specified Investments:

Institution	Maximum Investment per Group/Institution £M	Maximum Length	Credit Rating/Other Assessment of Risk
UK Banks	10 (£5M limit with any one institution)	Up to 2 years	As per Link's matrices and the Authority's definition of a high credit rating
Foreign Banks	2	Up to 2 years	As per Link's matrices and the Authority's definition of a high credit rating
Money Market Funds (max. of 5)	10	N/A	All are AAA rated
Other Local Authorities	10	Up to 5 years	N/A
<i>Note: Limits for Specified and Non-Specified are combined limits. The maximum limit will also apply to a banking group as a whole.</i>			

Appendix B

Economic Background

UK

December began with the Markit/CIPS Manufacturing Purchasing Managers Index (PMI) rising to 53.1 from 51.1 which had been the weakest since the referendum. On a positive note, the Construction PMI reading rose to a 4 month high of 53.4 spurred by house-building and commercial work. This confounded the consensus forecast of a fall to 52.5. The UK's dominant service sector's PMI experienced a shock slide and dropped to 50.4, the weakest since the 2016 Brexit vote and below all forecasts. Being the dominant sector, services dragged the Composite PMI figure down to 50.8 meaning overall activity was only just about maintaining growth.

GDP growth was unchanged at 1.5% year on year, with the month on month figure rising slightly to 0.1%, but both were below the forecasted increases. Alongside this, the GDP 3-month average growth to October dropped from 0.6% to 0.4%, emphasising that the impact of the positive Summer, which had been supported by good weather and one-off factors such as the World Cup, was now fading. Elsewhere, data shows that the UK's trade deficit rose above forecasts to £3.3bn in October, with the goods trade deficit also rising to £11.87bn.

Unemployment remained constant at 4.1% in the three months to October. With unemployment close to its lowest level since the 1970s, employers have begun to raise pay for staff more quickly. Average weekly earnings including bonuses rose by 3.3% on the year, the biggest rise since the three months to July 2008. This is the same figure recorded as the total earnings (excluding bonuses) for the three months to October. This allowed "real wages", which discounts the impact of inflation, to continue to grow as inflation fell to 2.3% year on year.

British retail sales surged by much more than expected in November, with the month on month figure coming in at 1.2%, up from the previous figure of -0.4%. The year on year figure came in at 3.6%, up from the previous figure of 2.4%. However, the Confederation of British Industry (CBI) data from the month was less bright. Mortgage approvals improved with the first year-on-year rise since September 2017 but the GfK consumer confidence reading fell from -13 to -14.

The UK recorded a lower than expected budget deficit in November. It fell to £7.2bn and for the first 8 months of the financial year, it stands at just under £33bn (30% lower than the same point in 2017). This is the lowest November borrowing for 14 years. Tax revenues remained strong but the government spent more than it received in tax and other income. National debt as a percentage of GDP stood at 83.9%, or £1.8 trillion.

In the US, the Nonfarm Payroll figure rose by 155,000, below the estimate of 200,000 and the previous downwardly revised 237,000. The final estimate of Q3 GDP was 3.4% trimmed slightly from the previous estimate of 3.5% but still above the economic growth potential of 2%. The Federal Reserve went on to raise the Federal Funds Rate to 2.25-2.5%, continuing the tightening cycle.

In the Eurozone, the European Central Bank (ECB) chose to continue to keep interest rates at 0% but the meeting spelt the end of its bond-buying programme as first announced in June. PMI figures improved from the previous month, but the final estimate

of Q3 GDP came in at 0.2% q/q and 1.6% y/y, both decreases from Q2's figures. Unemployment in the bloc remained at 8.1% in October 2018.

VAT - Key Performance Indicators:

Creditor Invoices

VAT return for	No of high value Creditor invoices checked	No of Creditor invoices highlighted as requiring "proper" document for VAT recovery	%age of creditor invoices checked requiring "proper" document for VAT recovery
Apr-18	130	17	13.08%
May-18	108	5	4.63%
Jun-18	169	11	6.51%
Jul-18	222	11	4.95%
Aug-18	220	18	8.18%
Sep-18	220	11	5.00%
Oct-18	273	8	2.93%
Nov-18			

Cash Receipting Entries

VAT return for	No of cash receipting entries checked by formula per the ledger account code used	No of cash receipting entries needing follow up check	%age of cash receipting entries needing follow up check
Apr-18	907	15	1.65%
May-18	810	8	0.99%
Jun-18	848	6	0.71%
Jul-19	499	10	2.00%
Aug-18	882	34	3.85%
Sep-18	529	5	0.95%
Oct-18	524	5	0.95%
Nov-18			

Debtor Invoices

VAT return for	No of Debtor invoices checked (value >£5k)	No of checked debtor invoices with incorrect VAT code used	%age of debtor invoices with incorrect VAT code
Apr-18	38	7	18.42%
May-18	50	4	8.00%
Jun-18	40	8	20.00%
Jul-19	57	11	19.30%
Aug-18	72	11	15.28%
Sep-18	64	5	7.81%
Oct-18	98	26	26.53%
Nov-18			

Purchase Cards

VAT return for	No of transactions for previous month for which paperwork requested for checking	No of Amazon invoices included in check	Resolvable errors discovered	No of transactions for which no response received within timescale	Value of VAT potentially claimable but recharged to budget due to non-response	No of transactions where VAT claimed incorrectly	%age of transactions available to be checked where VAT was claimed incorrectly	Value of VAT incorrectly claimed hence recharged to budget
Apr-18	260	13	12	6	£1,395.07	6	2.36%	£674.06
May-18	240	10	20	11	£1,127.77	15	6.55%	£563.64
Jun-18	440	15	14	9	£2,055.92	11	2.55%	£596.35
Jul-18	190	8	15	11	£2,003.66	8	4.47%	£300.39
Aug-18	107	4	5	5	£575.32	2	1.96%	£18.16
Sep-18	231	20	46	26	£3,664.29	25	12.20%	£1,936.26
Oct-18	251	18	22	18	£1,942.88	19	8.15%	£762.99
Nov-18								

Voluntary Declarations

Per HMRC regulations, any vat errors discovered can be adjusted in the current VAT account if they are:

- below the reporting threshold (>£10,000 or up to 1% of the VAT return Box 6 figure up to a maximum of £50,000)
- not deliberate
- for an accounting period that ended less than 4 years ago.

Any errors that do not meet these conditions have to be reported to HM Revenue and Customs and are referred to as voluntary declarations.

There are no voluntary declarations to date in 2018/19. However, Finance are currently looking at 2 areas where there appears to be incorrect vat accounting.

Chargebacks to service areas

As a result of the monthly Creditor invoice checking, Treasury Management produce a list of Creditor payments for which a “proper” vat document has not been received. Any VAT amounts on these invoices are held in the vat account and are not claimed until such time as a valid invoice is received. The relevant budget holder is emailed the details and asked to source a correct document. Failure to do this results in the relevant budget being charged with the vat amount that cannot be reclaimed due to the lack of a proper document.

Further to the above, the upload of appropriate documents to the Barclaycard purchase card system to enable vat recovery was made mandatory in September 2017 as a result of the lack of response from service areas/establishments to provide documents when

requested. Where no document has been uploaded, any VAT amount input against the transaction is charged to the service area as there is no evidence to support the vat recovery.

The total amount charged back to service areas in 2018/19 to date is £78,695.37. The breakdown of this is as follows:-

Reason	£
Not a tax invoice	14,822.52
Not a tax invoice – no response from service area	8,899.59
PCC not the named customer	14,900.24
No VAT registration number on invoice	93.20
No invoice uploaded to Barclaycard system	24,419.31
Invoices uploaded do not match the payment	1,011.71
No evidence supplied to enable vat recovery	6,397.07
Foreign VAT (not recoverable)	335.94
No VAT amount on invoice in first place	5,147.45
Supplier not vat registered	111.97
Supply not to PCC	1,054.29
Overaccounting for VAT	1,502.08

Of the above £70,543.64 was potentially recoverable. The majority of these errors are in respect of purchase card transactions. 36% of these errors were schools and 24% social care (including invoices for legal fees).