CYNGOR SIR *POWYS* COUNTY COUNCIL.

AUDIT COMMITTEE
9th May 2019

CABINET
21st May 2019

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

SUBJECT: **Treasury Management Qtr 4 Report**

REPORT FOR: **Information**

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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 March 2019.

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:

	Jun 19	Sep 19	Dec 19	Mar 20	Jun 20	Sep 20	Dec 20	Mar 21
Bank rate	0.75%	1.00%	1.00%	1.00%	1.25%	1.25%	1.25%	1.50%
5yr PWLB	1.90%	2.00%	2.10%	2.20%	2.30%	2.30%	2.40%	2.50%
10yr PWLB	2.30%	2.40%	2.50%	2.60%	2.60%	2.70%	2.80%	2.90%
25yr PWLB	2.80%	2.90%	3.00%	3.10%	3.20%	3.20%	3.30%	3.40%
50yr PWLB	2.60%	2.70%	2.80%	2.90%	3.00%	3.00%	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 the following investments at 31st March 2019:-

Invested with:	Principal £000's	Interest Rate	Start Date	Maturity Date
BOS	7,815	0.55%		
HSBC	1,145	0.50%		
Total	**8,960**			

4.3 Higher return rates have been 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 were 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 March 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 31.03.19:

	As at 31.03.18 Actual	2018/19 Current Actual	2019/20 Current Estimate	2020/21 Current Estimate
	£M	£M	£M	£M
Capital Financing Requirement	324,483	368,124	432,170	445,327

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.

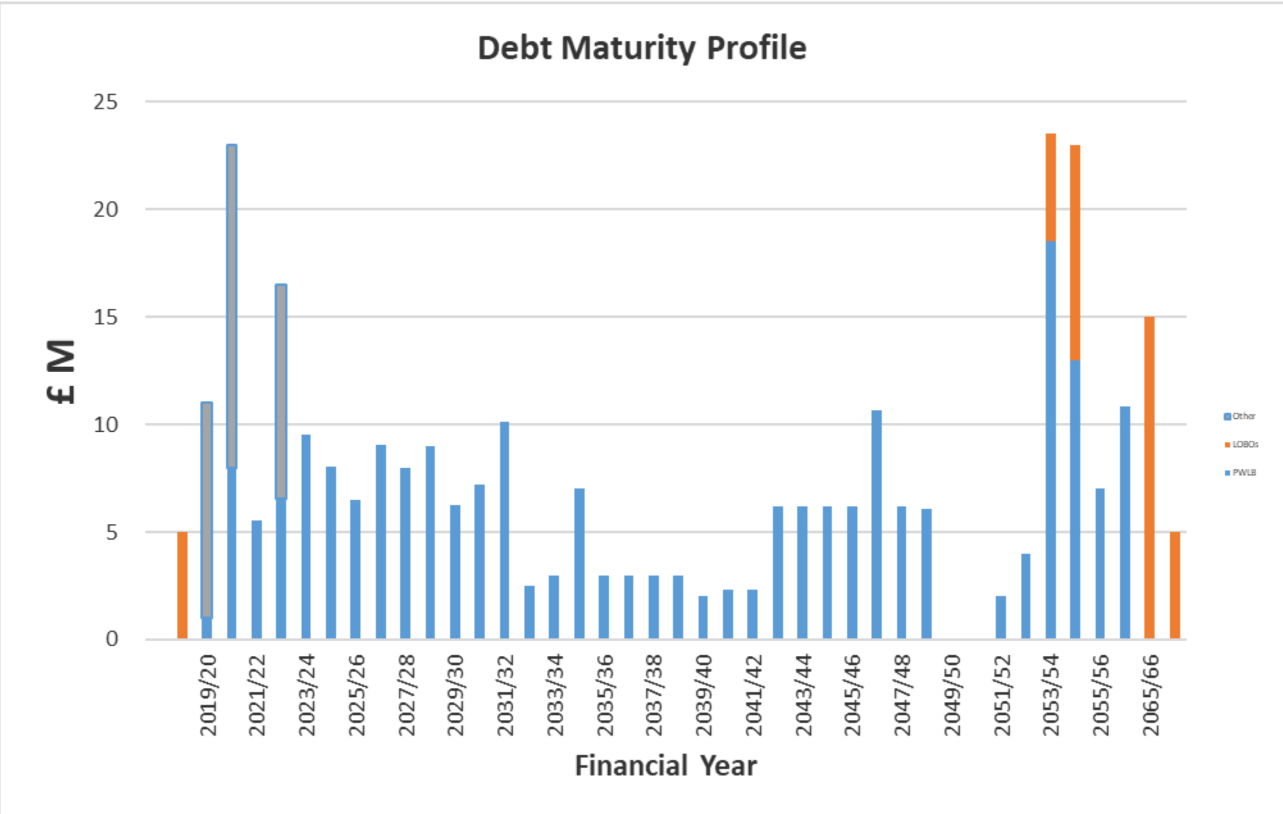
In line with this, £57.9m of longer-term borrowing has taken place in the 2018-19 financial year. The revenue cost of this borrowing was within budget and the first year annual effect of this new borrowing is £729k. This figure will decrease slightly year on year as a £20m loan included in the £57.9m is an EIP loan, whereby the principal is repaid equally year on year and hence the interest reduces in line with the decreasing principal.

6.4 Capital Budget/Spend per efinancials:

Capital:	**Approved Budget £**	**Working Budget £**	**Actual Capital Spend *(not including commitments)* £**	**%age Actual 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%
March (at time of report)		102,439,225	75,891,955	74.08%

The financing of the approved capital budget included £17.9m of Prudential borrowing in total.
It remains a significant challenge to manage the Authority's cashflow and its need to borrow when the Capital working budget continues to decrease significantly during the year and, despite this, actual spend is still significantly below the working budget.

6.5 *Debt Maturity Profile as at 31.03.19:*



6.6 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 March 2019.

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 March 2019.

8.3 Key Performance Indicators:

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

Members will see that, despite further advice and training provided to service areas, the amount of vat potentially recoverable totalled £105,087.63.

Further to this, £19,454.54 of errors took place whereby vat was incorrectly accounted for and had to be adjusted by Finance. This related to sample checking that took place as Finance do not have the resources to check all transactions. The time taken to do the current vat checking undertaken and any associated adjustments takes Finance time away from doing more proactive tasks.

These errors continue to be concerning, particularly as Making Tax Digital comes into being for local authorities in October 2019.

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:		Email:
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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

<u>Appendix A:</u>

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
Note: Limits for Specified and Non-Specified are combined limits. The maximum limit will also apply to a banking group as a whole.			

Appendix B

Economic Background

March began with the Manufacturing PMI which fell to 52 in February from 52.6 the previous month. Construction PMI dropped into negative figures falling to 49.5 from 50.6 the month before. This was caused by Brexit uncertainty and the slowing housing market delaying new building projects. Services PMI rounded the figures off with a rising score of 51.3 in February from a previous 50.1. This left the Composite figure at 50.3 from 51.5.

The UK's trade deficit continued to rise in January; the trade deficit in goods rose to £13.08bn and the overall deficit rose to £3.83bn, well above the forecasted £2.6bn.

One of the key economic indicators, CPI inflation, rose slightly in February to 1.9% y/y from 1.8% the previous month, moving closer to the Bank of England's 2% target. However, core inflation, which strips out the more volatile components, edged down to 1.8%.

The UK's labour market continued to defy forecasts; the unemployment rate fell to 3.9%, with employment increasing by 220,000, above expectations of 150,000. Meanwhile, wage growth excluding bonuses maintained its 3.4% y/y figure, with the overall figure falling from 3.5% to 3.4%. British consumers are currently enjoying a period of relief as "real wages" continue to be maintained, as wage growth is well above inflation.

A warm month of February caused retail sales figures to unexpectedly keep up their good start to 2019; retail sales y/y growth slowed slightly to 4% from January's 4.1% figure, well above forecasts of 3.3%, and showing that consumer spending continues to be a source of strength for the British economy at a time when Brexit uncertainty is looming over the nation. Prospects for retail sales continue to look strong as wage growth continues to exceed the pace of inflation. In another measure of nationwide consumer sentiment, GfK Consumer Confidence remained at -13.

On the 21st March, the Bank of England's Monetary Policy Committee (MPC) voted unanimously to keep the base rate on hold at 0.75%. Governor Mark Carney has remained dovish due to the prospect of Brexit, but did imply in his press conference that in case of a long Brexit extension, the MPC may move to raise rates in the summer.

The UK's public finances were once again stronger than expected as the resilient labour market boosted income tax revenue. Public borrowing for February fell to £0.2bn from £1.2bn a year earlier, below forecasts of £0.6bn. With just one month remaining of the financial year, government borrowing totalled £21.3bn, down 44% from the same point in the previous tax year, and the government is broadly on track to meet its fiscal targets. Alongside this, Chancellor Hammond suggested in his Spring Statement that spending on public services will be increased if an orderly Brexit can be achieved.

The Confederation of British Industry (CBI) data for the month was weaker than expected; the CBI Distributive Trades survey fell from 0 in February to -18 in March, despite being expected to rise to 5. The Industrial Trends survey also suffered a drop, from 6 in February to 1 in March.

To end the month, the final estimate of Q4 GDP growth showed a fall to 1.4% y/y from 1.6% in Q3. However, this is higher than the 1.3% earlier estimated. On the quarter, the UK achieved a final estimate of 0.2% growth, a fall from Q3's 0.7%.

In the USA, February’s Nonfarm Payrolls figure came in at just 20,000, a massive drop from 311,000 in January and below forecasts of 190,000. These numbers were amid a contraction in payrolls in construction among other sectors, raising concerns about a sharp slowdown in activity. This was also reflected in the final Q4 GDP estimate, which came in at 2.2%, a further downward revision and down from 3.4% in Q3. The Federal Reserve’s Open Market Committee (FOMC) chose to keep rates on hold as signs of a global slowdown start to take hold.

The Eurozone’s unemployment rate remained at 7.8% in January, below predictions of a rise to 7.9%. In terms of growth, the 3rd estimate of Eurozone Q4 GDP growth came in at 1.1% y/y, a sharp drop from Q3’s 1.6% figure, partly caused by the largest economy in the bloc, Germany, falling to nearly zero growth.

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	222	4	1.80%
Dec-18	189	11	5.82%
Jan-19	123	16	13.01%
Feb-19	187	10	5.35%
Mar-19	144	8	5.56%

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	540	15	2.78%
Dec-18	312	1	0.32%
Jan-19	751	1	0.13%
Feb-19	444	2	0.45%
Mar-19	908	11	1.21%

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	69	10	14.49%
Dec-18	78	6	7.69%
Jan-19	76	8	10.53%
Feb-19	96	8	8.33%
Mar-19	145	19	13.10%

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	378	44	26	22	£1,499.17	18	5.06%	£1,270.13
Dec-18	377	37	18	16	£2,411.11	21	5.82%	£1,410.98
Jan-19	272	27	16	12	£608.37	17	6.54%	£502.36
Feb-19	334	61	11	9	£658.92	14	4.31%	£422.59
Mar-19	487	41	38	26	£3,322.13	57	12.36%	£1,780.08

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 in 2018/19. However, Finance continue to look at 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 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 £124,542.17. The breakdown of this is as follows:-

Reason	**£**
Not a tax invoice	16,402.03
Not a tax invoice – no response from service area	10,783.95
PCC not the named customer	31,693.76
No VAT registration number on invoice	93.20
No invoice uploaded to Barclaycard system	36,521.00
Invoices uploaded do not match the payment	1,486.01
No evidence supplied to enable vat recovery	8,107.68
Foreign VAT (not recoverable)	441.05
No VAT amount on invoice in first place	6,145.16
Supplier not vat registered	111.97
Supply not to PCC	4,251.58
Overaccounting for VAT	4,738.60
PCC Internal payment	1.23
Document spoilt	2.00
Pool car adjustment	3,762.95
Total	**124,542.17**

Of the above £105,087.63 was potentially recoverable. The majority of these errors are in respect of purchase card transactions. 34% of these errors were schools, 35% social care (including invoices for legal fees), 7.83% Highways, 5.8% members and 5% Housing.